



# Peer monitoring in managing moral hazard

*An exploratory study on the functioning of peer monitoring arrangements on the management of moral hazard in the Dutch social housing sector*



**Cornelis Eikelboom**

*Master Thesis*





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*An exploratory study on the functioning of peer monitoring arrangements on the  
management of moral hazard in the Dutch social housing sector*

– Public version –

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*“It is the pressure of our peers that gives us the support to try things we otherwise wouldn’t have”*

**- Bill Treasurer -**

## Executive summary

### *Research problem: Can peer monitoring manage moral hazard in Dutch social housing sector?*

Many social housing corporations in the Netherlands are in financial distress because of excessive risk taking. The Dutch social housing sector is characterized by corporations providing mutual guarantees on the loans of one another, and consequently making corporations pay for one another in the case of serious financial distress (the ‘financial security structures’). A positive element of this risk sharing is that financing costs are relatively low. However, by this type of risk sharing, also moral hazard arises. In this research moral hazard is defined as strategic behaviour of an actor, from which the positive effects of risk taking are for the actor itself, while the negative effects are (partly) for others. Moral hazard is characterized by asymmetry in the information position between those engaging in risk and those carrying risk.

Literature argues peer monitoring, i.e. corporations monitoring one another, to be effective in managing moral hazard. Managing moral hazard is defined as limiting negative consequences of moral hazard whilst retaining its strengths. Peers are argued to have better information and be better capable to interpret information, thereby reducing the asymmetry in information characterizing moral hazard. Peers are argued to be willing to monitor one another, as this would reduce the negative consequences of their risk taking. However, recent claims on the financial security structures, suggest peer monitoring was ineffective. Therefore, this research answers the following question:

*What is the potential of peer monitoring to manage moral hazard between Dutch housing corporations and can this be improved?*

### *Aim and approach: Strengthen peer monitoring theory through an exploratory study*

Theory on peer monitoring is limited. Studies on peer monitoring mainly focus on its positive effects, but barely on its limitations. Hence, little is known of factors that potentially limit the effectiveness of peer monitoring in order to explore the potential of the financial security structures in the Dutch social housing sector in managing moral hazard. A literature study showed the context of the sector specific arrangements in peer monitoring to be very relevant. Therefore, the empirical element of this study is taken care of by an institutional analysis and exploratory case study. Driven by regulation literature and the distinction between the *willingness* and the *ability* of peers to monitor one another, this research is structured by five propositions:

- Peers have a sense of urgency to regulate one another
- Peers have information about each other’s behaviour
- Peers may interfere with each other’s business
- Peers have formal and informal means to intervene
- Peers have enough degrees of freedom to adjust regulation to the situation at hand

The study on the proposition underlines the high risk potential in the Dutch social housing sector and shows a low willingness and ability for peer monitoring because of barriers in the peer arrangement and in the sector context.

### *The Dutch social housing sector has many freedoms to engage in risk taking*

Dutch corporations are private organizations serving a public goal. Hence, they are positioned in between markets and governments. This limits the influence of the government on corporations, while corporations are protected from market incentives on effective and efficient allocation of resources.

Furthermore, legislation leaves much room for interpretation on activities corporations may engage in. The financial security structures allow corporations to finance their activities cheaply, but also to finance their projects relatively cheap and largely through loan capital. The opportunities to engage in risk taking are widened by guarantees on financing on the corporation level, without dedication to specific activities. In a time of economic prosperity and rising real estate values, this led to many risks being engaged in during the early 2000's. Hence, many freedoms in risk taking makes the Dutch social housing sector have a high risk potential.

### *Barriers in the peer arrangement result in a low willingness and ability for peer monitoring*

Four barriers inherent to the peer arrangements limit the functioning of peer monitoring in the Dutch social housing sector. First, peers have no ability to gather information of one another other than what is publically accessible. As peers are competitive to each other, they don't share much information voluntarily. Formal regulators produce public reports, but these do not provide the detailed information to monitor one another. Second, the sharing of risk over many peers reduces the willingness of peers to monitor one another, as the potential negative consequences for peers are limited. Third, the cost of peers to monitor one another is high, due to the quantity of peers to take into account. Fourth, corporations lack the tools to intervene at one another, further limiting the ability for peers to monitor one another.

### *Barriers in the sector context result in a low willingness and ability for peer monitoring*

As stated in literature in general terms, specific Dutch housing sector contextual factors turn out to be relevant for the potential of peer monitoring. Four categories of contextual factors are identified. First, as already discussed, peers have many freedoms to engage in risk taking. These freedoms reduce the willingness for peers to monitor one another. Second, the willingness to intervene at one another is hampered by the existence of formal regulators. Formal regulators take away the need for peers to regulate one another. Though formal regulators have tools to gather information and discipline corporations, peers currently cannot use them. Third, the network in which corporations operate reduces the willingness to regulate one another. Multiple interdependencies between corporations improve the ability to gather information one another, but reduce the willingness to intervene at one another. Furthermore, corporations are competitive to each other, thereby allowing each other to take on risk. The willingness to intervene is further limited by corporations as they respect one another as autonomous organizations. Fourth, a lack of precedents takes away the urgency for peers to regulate one another. Before 2010, no significant claim has been made on the security structures. Since 2010, the SGBB and Vestia cases made corporations more aware of their risks. This truly added to the willingness of peers to monitor one another. This results in all types of subtle peer monitoring arrangements starting to come into place.

### *Improvements for peer monitoring in managing moral hazard are limited*

Several alternatives for reducing the barriers on the functioning of peer monitoring in managing moral hazard, are identified. Some promising alternatives are 1) the monitoring of peers in smaller groups that are potentially self-formed and 2) an increase in the ability of peers to monitor one another either through legislation or closer cooperation to formal regulators. It is found that many alternatives may increase the willingness of peer monitor one another, but do so by increasing the moral hazard in the peer relationship. Identified alternatives on risk mitigation focus directly on the ability of risk taking. However, as a consequence these alternatives often limit the positive elements of moral hazard, and thus prove to be not very effective in improving the management of moral hazard.

### *Conclusion*

Horizontal regulation by means of peer monitoring may well have the potential to manage moral hazard better as compared to vertical regulation, but is currently lacking the ability and willingness to do so in the Dutch social housing sector. Barriers in both the design and the context of the peer arrangements prove to be decisive for the success of peer monitoring in this sector. Sharing of risk proves to be just one of the incentives influencing the willingness of peers to monitor one another. It is the total package of incentives that determines the willingness of peers to monitor one another. Paradoxically, many improvements that increase the incentive to regulate one another also strengthen the moral hazard in the peer relation.

Peer monitoring starts to show potential through very subtle arrangements since the economic crisis and the collapse of Vestia. However, peers who now experience the incentive to monitor one another do have insufficient ability to do so properly. Hence, the ability to monitor one another should be focussed at those having the incentive to monitor one another. Apart from peer monitoring, this notion holds for regulation in general.

The main strength of peer monitoring in comparison to vertical regulation is argued to be its potential to limit information asymmetry. More specifically, peers are argued to be better in giving availability to information in comparison to others. Currently, however, peers in the Dutch social housing sector do not have sufficient ability to gather detailed information. Peers themselves argue they are best capable to judge information of others. However, bound to the limited ability to gather information, the suggested strength of peer monitoring is not found in practice.

Thus, the potential for peer monitoring in managing moral hazard is limited in the way it is currently functioning in the Dutch social housing sector. However, recent developments indicate progress and may further free the potential of peer monitoring on the management of moral hazard in general in the future. For now, other alternatives for mitigating moral hazard can be thought of and are potentially more fruitful. However, these alternatives generally also hamper the positive effects of moral hazard.

### *Recommendations for further research*

This study highlights multiple factors that hamper peer monitoring in realizing its full potential in managing moral hazard. In line with regulation literature, the effectiveness of peer monitoring is found to be highly context dependent. Still, this is just a single study in a single sector. More case studies in other sectors are to be conducted to get a good overview of factors that influence the functioning of peer monitoring in general.



In the Dutch social housing sector, peer monitoring proves to be no direct substitute for vertical regulation. Both peer monitoring and vertical regulation have their relative strengths. Combining peer monitoring and vertical regulation might bring forward the best in both and mitigate the weaknesses of both. However, little is known on how the two are best combined. Further research in this field potentially develops a framework on how to combine the two best and consequently optimize the potential of peer monitoring.

In order to improve the functioning of peer monitoring in the Dutch social housing sector, this study identifies a number of alternatives. These alternatives are suggestions based on the empirical results of this study that need further research on their effectiveness, applicability and cost. Also, peer monitoring is not necessarily the only way to go in managing moral hazard. Therefore, for the Dutch social housing sector in specific, further research is needed in other ways to manage moral hazard better. For a start, it appears the moral hazard itself can be managed better by changing some of the conditions from which peers are enable to engage in risk.

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## Research Set up

in his or her blood. It is said to be spread to the blood of another person through a needle or syringe. It can be spread to other people through blood or symptoms are not. The specific behavior is not. HIV include:

- Having more than one sex partner (unless both sex partners are only with each other and are infected).

## 1. Introduction

Of the 7.2 million houses in the Netherlands (Bortel & Elsinga, 2007), over 30% (2.4 million) is owned by a housing corporation (CFV, 2012b), a share absolutely unique in Europe (SER, 2010). As a result from rebuilding the Netherlands after World War II, the equity of social housing corporations was build up mainly with government funding (Kempen & Priemus, 2002). By cutting the organizational and financial ties from the corporations with the government in the 1990s, housing corporations were made increasingly autonomous. In financial terms only a 'last line of defense' security function connects the government with corporations (Bortel & Elsinga, 2007). Corporations now have to operate in a market environment while serving a public goal. This puts a challenge on the corporations in terms of transparency and risk taking as they now fall in between governments and markets.

Over the last couple of years, multiple corporations came in financial trouble for a variety of reasons. Well known is Vestia, who established a portfolio of derivatives of €17,2 billion (gross value) based on pledges worth only € 5 billion (Hoekstra, Hoogduin, & Schaar, 2012). A corporation in Maastricht, engaged in the development of a new university campus, lost €75 million (Servatius, 2010a). Another corporation came in financial trouble because of land purchasing, at a certain moment in time having 200 hectares of bare ground while owning just 4000 houses, leading to a loss of over €60 million (Rijksoverheid, 2011; WSG, 2011). None of the activities mentioned above is illegal in itself, but the excessiveness transcends the risk they can bear. This excessive risk taking can be explained by a phenomenon that scholarly literature names 'moral hazard' (Eisenhardt, 1989a). Here, moral hazard is defined as 'strategic behavior of an actor, from which the positive effects of risk taking are for the actor itself, while the negative effects are (partly) for others.

Moral hazard is characterized by information asymmetry, i.e. the idea risk takers have more knowledge and information on their activities and the corresponding risks than others (Akerlof, 1970; Arrow, 1971). Information asymmetry and moral hazard are often described in a vertically oriented relation, i.e. there is someone (the 'agent') who undertakes an activity (e.g. social housing) for the 'principal' that has difficulties in monitoring the performance of the agent (Cowton, 2002).

Literature argues that information asymmetry is smaller in a horizontal setting. The idea is that corporations have similar information and knowledge as their peers, suggesting that peers are better able to regulate on peers that take on too much risk (Stiglitz, 1990). In this research, these horizontal arrangements are referred to as peer monitoring. In Dutch social housing, peer monitoring is shaped by letting each corporation pay for the financial support of a corporation given by either CFV (the financial supervisor) or WSW (the deposit guarantor of loans) in case CFV or WSW has to fund a loss at one of the corporations. Of course, this arrangement is embedded in culture and regulation and co-exists with other regulation. According to theory, corporations will perform this peer monitoring as eventual negative outcomes come at their own expense (Stiglitz, 1990; Brousseau & Glachant, 2011). However, recent history illustrates that theory differs from practice. Therefore, this research answers the following question:

*What is the potential of peer monitoring to manage moral hazard between Dutch housing corporations and can this be improved?*

In most scholarly literature, moral hazard has a negative connotation as others share in the negative effects of risk taking. However, moral hazard also has a positive side. In the Dutch social housing sector, corporations are capable to attract cheap financing because of the risk sharing. Hence, the risk sharing directly contributes to their objective of providing cheap housing (as it may save up to €35 per housing unit per month). It is for this reason, the main research question considers the potential of peer monitoring to mitigate the negative effects whilst keeping the positive effects, i.e. the potential to 'manage moral hazard'.

The answer to the main research question is found by performing a case study research on three corporations in the Dutch social housing sector. The content of the research is split into four parts: Research set up, theory, analysis and design. The research setup introduces the research (this chapter) and deepens on the problem; the research question as well as the approach, structure and relevance of the research are introduced in chapter 2.

In the theoretical part, scholarly literature on moral hazard and peer monitoring are analyzed. As the sector context proves to be relevant also other literature on (responsive) regulation and networks is studied. By the end of chapter 3, this results in five propositions that form the basis of this study. Given the characteristics of the research problem, a case study seems a useful approach and is therefore introduced in chapter 4.

The analysis part starts with an institutional analysis studying the moral hazard and peer monitoring in their regulatory and institutional context in chapter 5. This analysis leads to some first findings to the propositions identified in chapter 3. The case study in chapter 6 studies the specific situation for three corporations in the Netherlands. A comparison of these cases also contributes to results on the propositions. The results of the institutional analysis are brought together in chapter 7. This chapter also generalizes the findings of the case study to the functioning of peer monitoring in the Dutch social housing sector and describes the implications for using peer monitoring to manage moral hazard. Chapter 8 concludes the analysis part by discussing the validity of the results.

This study concludes with a prescriptive part. In this part (which entails chapter 9 and 10) alternatives that may improve the functioning of peer monitoring in the Dutch social housing sector are identified. After this chapter, conclusions of this study are formulated as well as recommendations for further research. A reflection concerning both the content and process of this study as well as a consideration on contemporary developments in the sector finalizes this research.

## 2. Research design

This chapter presents the design of this research. To do so, the first section deepens the understanding of the problem at hand, which results in the relevance of the project to be discussed in the second section. The questions this research is to answers discussed in the third section. The fourth section introduces the approach that is used to answer this questions. The Dutch social housing sector is a wide sector of which only one part will be the main topic of study. Therefore, section five clarifies the focus of this research. This leads to the structure of the research that is presented in the sixth and final section of his chapter.

### 2.1 Research problem

A core condition experienced by regulators is that they have to deal with asymmetric information. In ‘vertical’ regulation (i.e. an external and formal regulator like CFV) this creates opportunities for corporations to influence regulators (Bruijn & Heuvelhof, 2005). As corporations share costs when a corporation gets in serious financial trouble, also some form of ‘horizontal’ regulation could exist. Stiglitz (1990) argues that this horizontal regulation, which he calls ‘peer monitoring’, might contribute to regulation as the information asymmetry between peers is smaller.

This form of insurance also has a downside. When making an investment decision, a corporation makes a trade-off between revenues and risk. The above described insurance arrangement makes that organizations are supported when risks materialize, while benefits are kept when risks pay out. In other words, the insurance arrangement increases risk taken by corporations. Scholarly literature names this moral hazard (see chapter 3). Moral hazard is characterized by asymmetry in information between the risk taker and those regulating the risk. Peers are argued to have better information, and are thus better capable to manage moral hazard as the asymmetry in information is smaller.

First signs show that the effectiveness of peer monitoring on managing moral hazard could be in question. Over the last years, peer monitoring did not seem to function in the Dutch social housing sector as multiple corporations are in serious financial trouble because of excessive risk taking (Ministerie van Binnenlandse Zaken en Koninkrijksrelaties, 2013a). The aim of this research is to explore the effectiveness of peer monitoring on managing moral hazard.

This research is specified to the case of the Dutch social housing sector. The (potential) existence of peer monitoring is embedded in the sector culture. Peer monitoring is not the primary regulation arrangement on which the corporations depend. In fact, the sector has three regulators (CFV, BZK, and WSW) next to other organizations that monitor or report on the (financial) performance of corporations (Hoekstra, Hoogduin, & Schaar, 2012). Hence, peer monitoring is to function in a broader context. Contemporary scholarly literature indicates that it is important to consider regulation (and thus peer monitoring) in its context, because the context often brings complexities to regulation (Bruijn & Heuvelhof, 2005; Baldwin & Black, 2008).

### 2.2 Research relevance

A distinction is made between the scientific relevance and the social relevance of this study. Scientifically, little is known on the functioning of peer monitoring. Stiglitz (1990) describes a successful case of peer monitoring at the Grameen Bank of Bangladesh, but does not widely elaborate on the functioning of this arrangement. However, considering the importance of asymmetric information in moral hazard, peer monitoring seems a promising regulatory arrangement



(chapter 3). Still, the arrangement appears not to have functioned in the Dutch social housing sector. It is therefore scientifically relevant to explore factors that contribute to the (non-)functioning of peer monitoring arrangement.

Socially, the Dutch social housing sector is of great importance by providing housing for the (financially) weaker half of society. Materializing risks come at the cost of social capital of the corporation, or at the cost of the combined corporations (Aedes, 2012a). For example, until now Vestia cost the combined corporations €700 million (Hoekstra, Hoogduin, & Schaar, 2012), nearly €300 per housing unit in the Netherlands. Hence, preventing these situations in the future is very relevant. Peer monitoring seems promising but also seems to non-function in its current form. Hence, it is also very relevant to explore factors that improve or hamper this arrangement.

## 2.3 Research questions

The aim of this research is to explore the effectiveness of peer monitoring on managing moral hazard. Therefore, peer monitoring (as being a regulation arrangement) is considered in its institutional context. This forms the basis for the main research question to be answered in this research:

*What is the potential of peer monitoring to manage moral hazard between Dutch housing corporations and can this be improved?*

To answer this question in a structured way, the main research question is supported by a number of sub questions:

### *Theory*

- a) How may peer monitoring contribute to managing moral hazard?
- b) What is the power of context for peer monitoring in managing moral hazard?

### *Analysis*

- c) Do corporations have the willingness to regulate one another?
- d) Do corporations have the ability to regulate one another?
- e) What are interactions of peer monitoring with its environment?

### *Improvement*

- f) What are possible improvements for the functioning of peer monitoring in the sector?

## 2.4 Research approach

To answer the research questions, a qualitative exploratory research is performed. The research is qualitative as literature, policy documents and interviews will be the main data sources, as is shown in chapter 4. The research is exploratory as the research aims to provide explanations on the functioning of peer monitoring in managing moral hazard. The approach of this research consists of three elements: a scholarly literature review, an institutional analysis and a case study. The elements are selected as they are able to deal with the specific characteristics of this study: boundaries between phenomenon and context are unclear and contextual conditions are relevant.

### 2.4.1 Scholarly literature review

The literature review consists of three elements. First, attention is given to the phenomenon of moral hazard. Apart from defining moral hazard for this research, this comprises elements as the core conditions for moral hazard to occur. Secondly, peer monitoring literature is studied as being the regulatory arrangement of this study. Special attention is given to the ability of peer monitoring to manage moral hazard. Therefore, peer monitoring as potential regulatory arrangement is studied in the context of regulation theory. Traditionally, regulation is considered in a single 'vertical' relation between 'regulator/inspector' and 'regulatee/inspectee'. However, as is recognized in contemporary regulation literature, reality is more complex. This makes it necessary to also study regulation theory in its context, found in network theory. The literature review is schematically represented in figure 2.1. Through the literature review, a broad understanding of the ability of peer monitoring to manage moral hazard is created. Also, the knowledge gained in the literature review will form the basis of the propositions used in the case study.

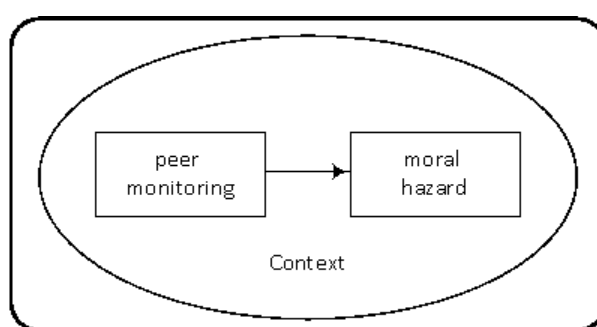


Figure 2.1: Schematic representation of unity in the literature review

### 2.4.2 Institutional analysis

The institutional analysis concerns the studying of how social structures and mechanisms function according to both empirical and theoretical rules in the financial domain of the Dutch social housing sector (Aoki, 2001). The functioning of both peer monitoring and risk taking in the Dutch social housing sector is inspired by the sector culture, embedded in sector regulation and shaped by interactions with a variety of organizations. Through the institutional analysis, the impact of these types of arrangements on moral hazard and peer monitoring is assessed. The institutional relevance is further elaborated on in section 3.4. By studying the sector culture, legislation and actor network corporations operate in, the propositions identified in section 3.5 are discussed.

### 2.4.3 Case study

A case study is a good method for studies where the boundaries of the phenomenon are unclear and the context is relevant (Yin, 1989). The case study is used to discuss the propositions identified in section 3.5. In chapter 4, the appropriateness for using a case study is discussed further. It is here relevant to say that to study the function and effectiveness of peer to peer arrangements on the management of moral hazard, three corporations are studied.

## 2.5 Research focus

Moral hazard may occur in many places and in many circumstances. Traditionally, moral hazard is often considered in an agency dilemma, i.e. when a party (the ‘agent’) acts in the interest of another (the ‘principal’), where the two are not fully aligned in goals and/or risk preferences and information asymmetry and uncertainty are existing (Eisenhardt, 1989a). It is argued that peers have similar knowledge and expertise, thereby knowing better what information to look for and how to interpret that information. Hence, peers theoretically have the opportunity to reduce information asymmetry (Armendáriz de Aghion, 1999). Peers may thus be in a better position to discipline each other. What this study names ‘peer monitoring’, appears to be the regulatory arrangement of choice. Hence, as already discussed in the previous sections, regulation theory seems appropriate to study the peer monitoring potential. In regulation theory, one can consider the regulator to act as the principal where the ‘regulatee’ can be considered an agent (Bruijn & Heuvelhof, 2005). Considering peer monitoring, one might consider the peers as principal and the peer monitored entity as agent. This leaves many (though not all) relations sensitive to moral hazard.

In the main research question, the research domain was already delineated to the Dutch social housing sector. In section 2.2, it was already hinted that special attention is given to the financial domain of the sector. As discussed in the previous section, peer monitoring is considered in the context of regulation and regulators in place. Still, multiple relations sensitive to moral hazard now remain. Being interested in the functioning of peer monitoring on managing moral hazard, the focus lies on the moral hazard relationship between peers, i.e. corporations. This is schematically depicted in figure 2.2.

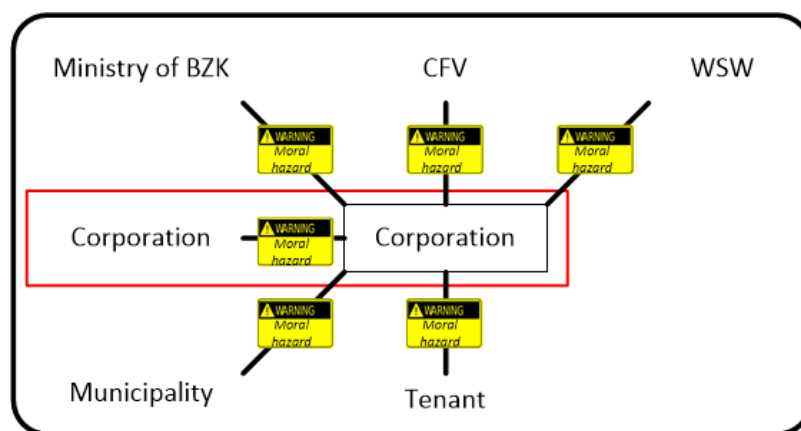


Figure 2.2: Corporation to corporation is the main moral hazard sensitive relation of interest

## 2.6 Research structure

This research consists, apart from this research set up, of three parts and is schematically represented in figure 2.3. In the first part, literature, the focus lies on the discussions in scholarly literature on what is moral hazard and how peer monitoring can be an effective regulatory arrangement to manage moral hazard. As peer monitoring appears to have no prime role in Dutch social housing regulation, the relationship between peer monitoring and moral hazard is studied in the regulatory context. As will be shown, contemporary literature on (responsive) regulation argues to also take the context of regulation into account. Therefore, the network context of regulation is also considered. The result of the literature review comprises a number of propositions that form the basis for the empirical study of the relationship between peer monitoring and moral hazard.

The second part, analysis, discusses the functioning of the propositions in practice. A preliminary discussion on the propositions is based on an institutional analysis. The institutional analysis studies how social structures and mechanisms function according to both written and unwritten rules in the financial domain of the Dutch social housing sector. As such, the institutional analysis can be seen as the practical application of the literature part. The result of this analysis part comprises factors that seem to influence the effectiveness of peer monitoring in managing moral hazard. To deepen the influence of these factors on the propositions, a case study is performed. This case study deeper explores the functioning of peer monitoring in managing moral hazard for the case of three corporations. Various documents and interviews will serve as input for the case studies. Various documents and interviews will serve as input for the case studies.

As such, the analysis findings provide the input for the third part: Improvements. Reflecting back on theory and the empirical analysis, this third and final part provides a number of prescriptive suggestions to the functioning of peer monitoring for managing moral hazard in the Dutch social housing sector. For each suggestion, some opportunities are sketched that may improve the function of peer monitoring in the Dutch social housing sector. Also, contemporary sector developments are reflected on.

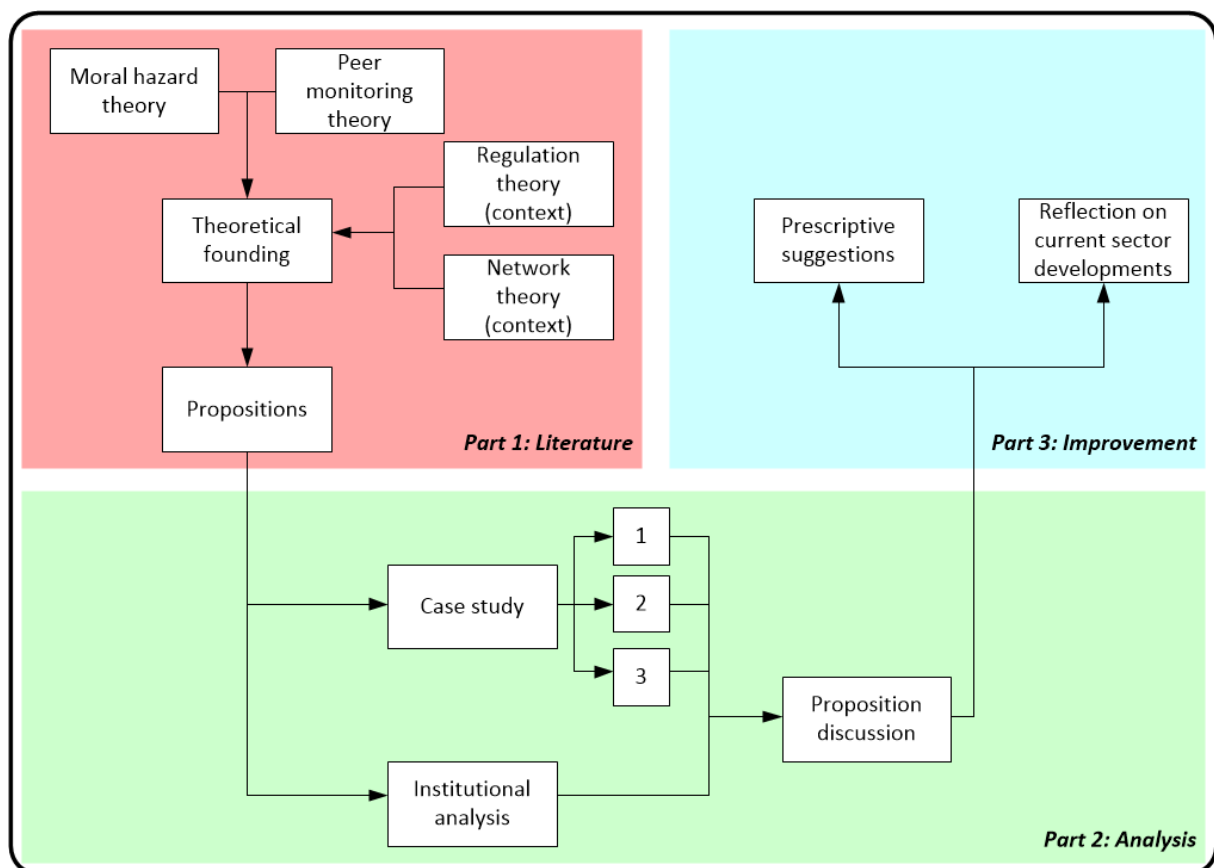


Figure 2.3: Research structure



## Part I – Literature



### 3. Theoretical founding

This chapter studies the potential of peer monitoring in managing moral hazard as described in scholar literature. The coherence of this chapter is depicted in figure 3.1. This first section zooms in on the concept and preconditions of moral hazard to come to a definition. The potential role of peer monitoring for managing moral hazard is deepened in the second section. As context proves to be relevant, the third section deepens on regulation literature where the fourth section deepens on the relevance of the network context. This literature study results in five propositions on the functioning of peer monitoring that are discussed in the fifth section.

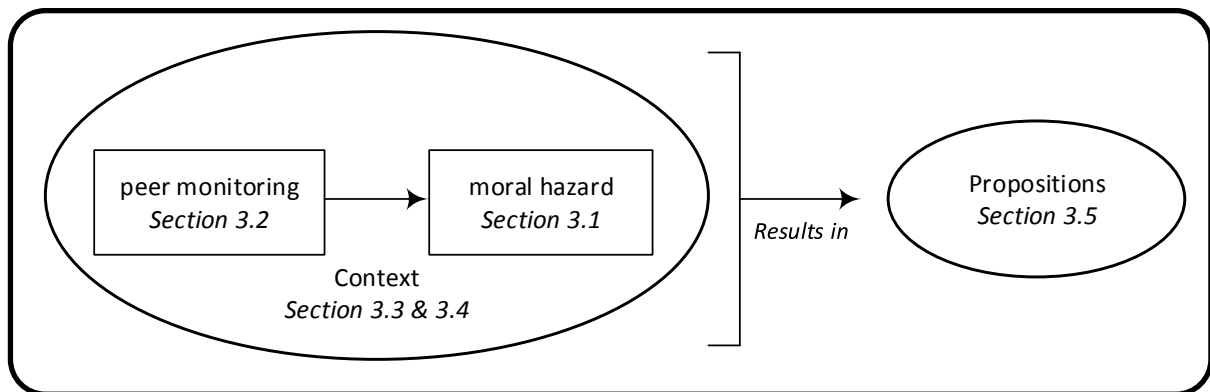


Figure 3.1: Coherence of the chapter

#### 3.1 Moral Hazard

In the introduction, moral hazard was defined as strategic behaviour of an actor, from which the positive effects are for the actor itself, while the negative effects are (partly) for others. In this section this definition is elaborated on further, by studying the core concept and preconditions of moral hazard, as well as the variety of definitions used. Subsequently, it is shown that although moral hazard often has a negative connotation, it also has (or is consequence of) positive elements.

##### 3.1.1 Core concept

Moral hazard occurs when a party has a tendency to behave inappropriately from the perspective of another party, while the latter is bearing (a part of) the (potential) negative consequences. Where the term originally was implying fraud or immoral behaviour, this is less so since it is a renewed subject of study (Dembe & Boden, 2000). Economist now use the term to describe inefficiencies when risks are displaced or cannot be fully evaluated (Klick & Mitchell, 2006).

Moral hazard is mainly used in the fields of insurance, finance, economic theory and social sciences. The usage of the term 'moral hazard' originates in the insurance industry, where insurers worried that their insurance might make the insured act in a riskier way because of his insurance (Dembe & Boden, 2000). This makes that two types of moral hazard can be distinguished: ex-ante and ex-post (Hellmann, Murdock, & Stiglitz, 2000). Ex-ante moral hazard refers to the idea that moral hazard has effect on the probability of a risk materializing. For example, housing corporations may take on more risk, as the negative consequences are covered by others. Ex-post moral hazard refers to the usage of the 'insurance'. For example, the existence of the external coverage of risk may cause corporations to invoke this coverage earlier, instead of dealing with the loss internally.

### 3.1.2 Preconditions

Three different preconditions of moral hazard can be identified: separation of ownership, asymmetry in information and a concept called 'hidden action'. It lies within the very core concept of moral hazard that the actors experiencing the positive consequences of a risk are not the same as the ones experiencing the negative consequences (Eisenhardt, 1989a). It is for this reason that, in the definition used in this research, an explicit distinction is made between 'the actor who causes moral hazard' and 'others'. Because separation of ownership is such a basic and straightforward concept, it is not further discussed here.

The second precondition of moral hazard is the existence of information asymmetry. It is because others don't have the same information available (or cannot give meaning to that information) that actors are capable to engage in these risks (Arnott & Stiglitz, 1988). Information asymmetry makes that moral hazard often arises in principal-agent problems (Arrow, 1971). What makes moral hazard different, is the third precondition: hidden action.

Holmström describes the concept of hidden action as follows: 'moral hazard may arise when individuals engage in risk sharing under conditions such that their privately taken actions affect the probability distribution of the outcome' (Holmstrom, 1979). In hidden action, it is the actor that has the information that takes on risk. Hence, it is also this concept what distinguishes moral hazard from adverse-selection (based on 'hidden information', i.e. the actor taking on the risk is unaware of some information that is held back by the seller of the risk). The importance of hidden action in moral hazard recently became clear in the subprime mortgage crises (Lewis, 2007; Krugman, 2009), where 'the risks ... became so widely dispersed that no one was forced to worry about the quality of any single loan' (Zandi, 2009). This insinuates that moral hazard comes to existence through concrete actions, though these actions are not necessarily made with the awareness of the risk change caused by the action, i.e. the consequence. This is further elaborated upon in paragraph 3.1.3.

It is the combination of these preconditions, especially the information asymmetry, that make moral hazard hard to observe (Holmstrom, 1979). As a consequence, it is also hard, if not impossible, to proof that moral hazard is existing in the Dutch social housing sector. There are, however, two arguments to consider the contemporary developments in the Dutch social housing sector as moral hazard. First, the scale on which corporations experience significant financial issues (not even considering those who are forced to significantly cut in their social capital (i.e. BMV, see appendix I)) makes it unlikely that these corporations are only outliers. Second, even though the current economic climate appears a trigger for corporations to get in financial trouble, it is generally not seen as a cause. Also, the concept of moral hazard seems to match contemporary sector developments. As such, it is at least useful to consider contemporary developments in the Dutch social housing sector as moral hazard.

### 3.1.3 Defining moral hazard

The variety of definitions used for moral hazard seems to focus itself on two axioms. As moral hazard can be seen as behaviour or as outcome/result, the perspective of this research on moral hazard in respect to these concepts is discussed first. Second, the awareness of moral hazard actions is discussed. These two elements combined provide the argumentation for why moral hazard is here considered as 'strategic behaviour of an actor, from which the positive effects are for the actor itself, while the negative effects are (partly) for others'.

### *The difference between actions and consequences*

In the previous paragraph (3.1.2) two seemingly opposing definitions of moral hazard were used. Holmström speaks of moral hazard ‘when individuals engage’ (Holmstrom, 1979), thereby implying moral hazard is some type of behaviour. Klick and Mitchell, speak of moral hazard more as a result when they define it as ‘inefficiencies that occur when risks are displaced’ (Klick & Mitchell, 2006). More abstract, it seems like moral hazards is studied either as action (Holmstrom, 1979; Dembe & Boden, 2000; Fang & Moscarini, 2005; Heuvelhof, Jong, Kars, & Stout, 2009) or as consequence (Klick & Mitchell, 2006; Pauly, 1968). These two ‘perspectives’ make four different views on moral hazard risk exist. These are schematically represented in figure 3.2. Tension exists in the views on moral hazard where the two perspectives oppose each other (situation 2 and 4) in their finding of moral hazard.

In perspective 2 of figure 3.2, inefficiencies occur by the displacement of risk. However, the specific action that made ‘individuals engage in risk sharing’ is not recognized. This situation shows the importance in the actions perspective to define ‘action’ (or, following Holmström, to define ‘engage’). Conceptually, the question is whether or not the decision on taking or not taking action can be considered an action in itself. For example, when the investment environment decreases, but a corporation does not adapt its risk taking profile, can this non-decision be considered an action? This shows that there is a grey area between situation 2 and 3, depending on the definition used. The next subparagraph elaborates on what is considered an action in this research.

In perspective 4 of figure 3.2, the ‘action’ perspective considers moral hazard to be existent, though the consequences did not (yet) manifest. This situation shows a limitation of the consequences perspectives, as it tends to only consider risks that have materialized, not risks that did not (yet) materialize.

no moral hazard action No moral hazard consequence 1	no moral hazard action moral hazard consequence 2
4 moral hazard action no moral hazard consequence	3 moral hazard action moral hazard consequence

Figure 3.2: Different views on moral hazard based on actions and consequences

The focus of this study lays in the vulnerabilities on the avoidance of moral hazards and not on the materializing of, what is here considered, moral hazard. For that reason this study uses the action based ‘perspective’, i.e. focus on the behavioural aspect, but keeping in mind the consequences on the system level.

### *Awareness of actions*

Issues concerning moral hazard were traditionally studied in the field of insurance, with the idea that protecting clients from risks might encourage those clients to behave in riskier ways. Base principle in this approach is that this was done fully intended (Dembe & Boden, 2000). However, it seems

unlikely that firms systematically and explicitly discuss the moral hazard consequences of their decision making.

Krugman defines moral hazard as ‘any situation in which one person makes the decision about how much risk to take, while someone else bears the cost if things go badly’ (Krugman, 2009). This rather broad definition allows for both intended actions as well as unintended actions and actions because of indifference. Unintended actions and actions of indifference, as described in the subfield or morale hazard (Dembe & Boden, 2000; Fang & Moscarini, 2005), do not seem to fit in the contemporary actions of firms (Hellmann, Murdock, & Stiglitz, 2000; Zandi, 2009) and doesn’t respect the second core assumption of ‘hidden action’. However, hidden action might have unintended consequences. This latter option is suggested by Ten Heuvelhof et al, who defined moral hazard as ‘behaviour of the agent after the adoption and coming into effect of the arrangement. ... The agent to whom the performance agreements apply will make sure he scores a flattering, good assessment by means of hidden actions, even though this performance is less satisfactory on closer inspection’ (Heuvelhof, Jong, Kars, & Stout, 2009). It is based on this definition that, in this research, moral hazard is considered strategic behaviour by which a firm tries to maximize its own gains.

Strategic behaviour can take many forms. In any firm, the executive board is responsible for actions taken by the firm. Other than the more intended forms of strategic behaviour, one could argue that sloppiness is also a form of strategic behaviour by the firm as the executive board neglects its responsibility for the internal governance. Reflecting back on the previous paragraph, the notion of executive responsibility suggests non-decisions are to be considered actions as well.

It is the combination of considering moral hazard from an ‘actions perspective’, and the consideration of classifying non-actions as actions as well, that moral hazard is here defined as: ‘strategic behaviour of an actor, from which the positive effects of risk taking are for the actor itself, while the negative effects are (partly) for others.

#### **3.1.4 Negative connotation, but positive aspects**

Since the use of the term moral hazard by insurance economists, it has a negative connotation (Eisenhardt, 1989a; Pauly, 1968; Hellmann, Murdock, & Stiglitz, 2000; Krugman, 2009). Moral hazard has this negative connotation as it is argued to have cost inefficiencies as an effect (Nyman, 1999). However, it should be noted that there are also positive aspects which are related to moral hazard. Two types of positives aspects are distinguished: efficient moral hazard and positive action that have moral hazard as a downside.

Nyman (1999) argues that moral hazard that has a positive effect exists as well. As an example, he argues that the ‘over consumption’ of medical care might have the consequence of making individuals more productive and living longer, thereby bringing net benefit to the societal welfare. This is what Nyman calls an ‘efficient moral hazard’. Following this reasoning, moral hazards in Dutch social housing could be efficient when the materializing of a moral hazard in the long term makes corporations act more efficient in their investments, thereby still gaining net benefit.

Second, moral hazard is often the consequence of a socially preferred (i.e. ‘positive’) action of risk sharing (Holmstrom, 1979; Boadway, Leite-Monteiro, Marchand, & Pestieau, 2006). For example, you might sport less when they do not have a health insurance as sporting increases the risk on potential injuries or you might not drive your car when you will be held accountable for all damage in an

accident etc. This also partly applies to Dutch social housing (SER, 2010). Through WSW, the organization that provides guarantees on corporation loans, the risk sharing over corporations enables these corporations to attract loans with a low interest rate. This cheap way of financing enables corporations to engage in more activities, thereby positively contributing to their public goal (Priemus, 2011). As a consequence for this research, it is important to realize that these positive elements are also existing, i.e. the goal is not necessarily to remove all moral hazards from existence. Therefore, 'managing moral hazard' is, as discussed earlier, considered to be mitigating its weaknesses whilst protecting its strengths.

### 3.2 Peer monitoring

Earlier, it was argued that a core precondition of moral hazard is information asymmetry. It was also argued that peer monitoring may contribute to limit the asymmetric information. This section introduces the contemporary subject of study that addresses the potential of 'horizontal' arrangements in effectively managing moral hazard. As the design of these arrangements have long been ignored by scientific literature, it is a contemporary field of study (Stiglitz J. , 1990; Brousseau & Glachant, 2011).

The concept of peer monitoring will be clarified in an example: The Grameen Bank in Bangladesh provides loans to self-formed groups of farmers that are mutually responsible for the loan. Other group members can only get credit once existing loans are repaid. In this way, Grameen Bank exploits local knowledge and created an incentive structure in which other members in the village monitor for the bank, thereby achieving a default rate of just 2% in contrast of the 60-70% of others (Stiglitz J. , 1990).

So, the basic idea is that there is 'dependence of one agent's utility on others' effort' (Arnott & Stiglitz, 1991), i.e. (created) interdependencies. In fact, opposed to the traditional 'vertical' principal-agent arrangements, a 'horizontal' arrangement is designed that may either replace or complement the vertical arrangements. In agency literature, these horizontal arrangements are described by a variety of names. Here, the term 'peer monitoring' is used.

Peer monitoring can be defined as those arrangements that incentivize peers (i.e. other agents) to monitor each other. Obviously, this definition allows for a whole range of arrangements that may vary in their obligation to participation, risk sharing etc. Still, this definition suffices the needs of this research. The value of peer monitoring lies in the 'presence of costly information' (Stiglitz J. , 1990). As moral hazard is a phenomenon of information asymmetry, characterized by hidden action, peer monitoring might contribute to managing moral hazard. This is based on the idea that peers have more (or 'cheaper') information on each other's behaviour, and/or are better capable of judging information of each other (Arnott & Stiglitz, 1991).

In the case of the Grameen bank, the interdependence required for the peer monitoring arrangement is artificially created (Stiglitz J. , 1990). This is similar in the Dutch social housing sector, where corporations are financially interdependent by law (Rijksoverheid, n.d.b), and are therefore required to have a liquidity buffer.

In studying peer monitoring as a replacement for the more traditional 'vertical' monitoring, Stiglitz (1990) came up with two valuable conclusions on preconditions for efficient peer monitoring. First, risk sharing appears to be more effective in relative small groups. Sharing of risk over large groups

creates a free rider problem. Each peer wants other peers to monitor the rest, and each peer has (relatively) many other peers to monitor. Even besides the free rider problem, monitoring incentives are minimal as the risk is widely spread. Secondly, having self-formed groups might be important as these groups form on comparable risk profiles (as no low risk peer group would allow a high/unknown risk peer in its group). This implies that peers in these groups also have the information needed to assess each other in terms of risk (Stiglitz J. , 1990).

### **3.3 Peer monitoring as regulatory strategy**

The previous section identified peer monitoring as a potential arrangement for managing moral hazard. As such, peer monitoring was introduced as an alternative/additional form of regulation. Classifying peer monitoring as 'regulator' makes that peer monitoring should also be considered in a regulation context. Therefore, this section starts with defining the general activities of a regulator. Subsequently, regulation theory on the compliance of agents is discussed. Two approaches are distinguished: deterrence and compliance (discussed in the second paragraph). In responsive regulation theory, discussed in paragraph three, it is argued that a combination of both approaches should be used. Concluding, critiques on responsive regulation argue that regulation should be considered in its context as well.

#### **3.3.1 Regulator activities**

Regulation concerns a number of activities. Bekkers et al (2002) name three activities of a regulator: the collection of information, judging on the information and, if necessary, intervening based on the judgment of information. Others, like Hood et al (2001), distinguish between a 'director' (a standard), 'detector' (information) and 'effector' (enforcement mechanism) function that are required for effective regulation.

Both activity categorizations are similar. Hood implies judgment in the effector, the effector/sanction that is based on the combination (i.e. the judgment) of a norm (director) and corresponding information (detector). Bekkers implies the existence of a norm as the basis for a sanction.

Often, the legislator is the setter of a norm. Hence, the setting of a norm is no core activity of a regulator in the sense of a supervising entity. In practice, however, legislation often leaves room for interpretation. Regulators are to anticipate on this leverage. As such, norm setting is a very relevant activity for regulators (Mertens, 2006). This research follows Hood (2001) in its classification of regulator elements: director, detector, and effector.

#### **3.3.2 Deterrence vs. compliance**

Traditionally, a distinction is made between two regulation approaches/styles: deterrence and compliance. The basic idea of deterrence is that an infringement of a rule should be penalized. As a result of this penalty, an agent will comply with the rules in the future (Baldwin, Cave, & Lodge, 2012). This type of regulation is seen all around us, think for example of speeding tickets, theft, or cartelisation. Central aspect here is that the enforcement of a rule is key. This makes the context of enforcement unambiguous. Information is crucial to the regulator (principal), as without information it will be hard to sanction and enforce appropriately. Because of the importance of information, and the unambiguous context, the relation between 'inspector' (regulator/principal) and 'inspectee' (agent) is relatively hierarchical (Bruijn & Heuvelhof, 2005).

Deterrence does not directly influence the morality of the regulated behaviour, it just punishes non-compliance. Literature argues that, therefore, deterrence often fails to improve compliance as sanctions will either not be big enough to avoid rational misconduct, or be so big that innocent bystanders are harmed (Parker, 2006).

The second approach is that of compliance. In this approach, gentle persuasion is to secure complying agents (Ayres & Braithwaite, 1992). This makes that regulators should invest in their relation with inspectees. Eventual compliance is a result of negotiations between the inspector and inspectee. Advantage of this approach over the deterrent approach is that it allows for ambiguity in the context and the non-hierarchical bilateral relation between inspector and inspectee (Bruijn & Heuvelhof, 2005). Disadvantage is that inspectors have the risk to 'comply' with the inspectees, i.e. are captured by the games that are played by the inspectees.

### 3.3.3 Responsive regulation

Back in the 80s, most regulation scholars seemed to follow the deterrence approach whereas most regulators seemed to follow the compliance approach. This led to scholars accusing regulators of how captured they are in practice, whereas regulators would accuse scholars of how out of touch they were. This camp settled by the question of how to balance the two approaches, leading to the theory of responsive regulation (Ayres & Braithwaite, 1992).

One of the core assumptions underlying the two traditional approaches is whether regulation has to be tailored for 'bad men' (deterrence, as people try to evade the legal structures of society) or 'good men' (compliance, as people look to law as a guide for proper action). By rough measures, it appears that 20% will comply with any rule, 5% will evade it, and the remaining 75% will comply if the punitive threat to the 5% evaders is credible (Kagan, 1994), showing the importance of motivational complexity in effective regulation (Ayres & Braithwaite, 1992). From this, it follows regulation should be capable to be both ferocious and forgiving: 'regulators will be more able to speak softly when they carry big sticks. Paradoxically, the bigger and the more various are the sticks, the greater the success regulators will achieve by speaking softly' (Ayres & Braithwaite, 1992).

The bigger the stick, the better (Ayres & Braithwaite, 1992). However, carrying just one big stick seems not sufficient. The problem is that the big stick imposes such a drastic sanction, it will only be used for the most extreme of infringements. Hence, a hierarchy and variety of sanctions is needed to reach compliance (Baldwin, Cave, & Lodge, 2012). Ayres and Braithwaite (1992) speak of a 'hierarchy of interventionism in regulatory styles', a concept they work out in what they call 'enforcement pyramids'.

Ayres and Braithwaite (1992) distinguish between an enforcement pyramid for sanctions (i.e. on the organization level) and for strategies (i.e. on the industry level), both sharing the same concept. Examples of enforcement pyramids are shown in figure 3.3 and figure 3.4. In the pyramid, means are ranked based on the pressure they exert on inspectees (Bruijn & Heuvelhof, 2005). An example of a hierarchy in sanctions for housing corporations is that they will receive a warning letter and chance for improvement before they will be appointed to the minister (chapter 5). Concerning strategies, a good example of self-regulation in the sector is the way the ministry allowed the sector to come up with systems for peer-funding to limit the excess equity of corporations. When the lower levels of the pyramid (like self-regulation) do not have the intended effect, the possibility (threaten to) to climb to the next step in the pyramid is there (Bruijn & Heuvelhof, 2005). As example, the ministry



used the benign gun as it threatened with regulation to limit the excess of equity of corporations (see chapter 5). Note that, in both pyramids, the possibility should also be there to get to a lower status in the pyramid again. Hence, a game is played between inspector and inspectee (Bruijn & Heuvelhof, 2005).

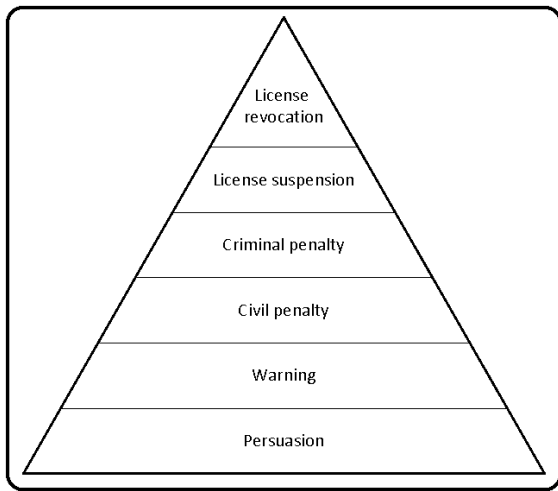


Figure 3.3: Sample enforcement pyramids of sanctions (based on Ayres & Braithwaite, 1992)

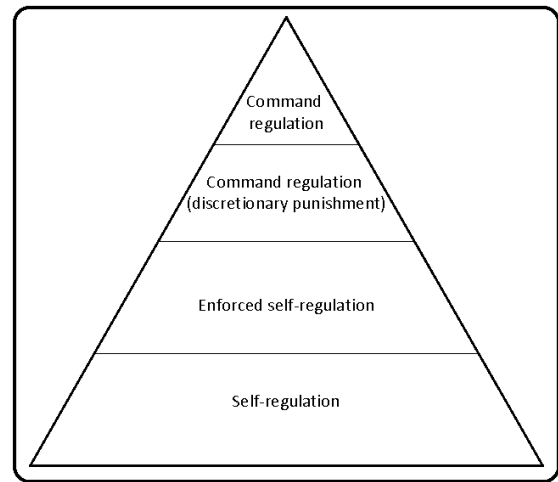


Figure 3.4: Sample enforcement pyramids of strategies (based on Ayres & Braithwaite, 1992)

Using 'enforcement pyramids' brings three main advantages. First, a well varied pyramid prevents over-enforcement (i.e. using too heavy means to bring a firm to compliance). Apart from over-enforcement being inefficient, it may damage the legitimacy of the inspector. Secondly, starting with lower sanctions is reasonable as it gives the inspectee opportunities to comply. This way, there are less opportunities for the inspectee to complain about the lack of chances to comply. Third, the 'shadow of sanctions' may bring firms to comply (Bruijn & Heuvelhof, 2005). Ayres and Braithwaite argue that successful cooperative regulation is predicted by three factors. First, the compliance approach identified in paragraph 3.3.2 as basis. Second, access to a hierarchical range of sanctions and interventions in regulatory styles. Third, the punitiveness of the most severe sanction (Ayres & Braithwaite, 1992).

Responsive regulation mainly focuses on the sanctioning activity of the regulator (regimes). However, a core condition of moral hazard (and many agency problems in general) is the asymmetry in information. This creates the opportunities for inspectees to influence inspectors/regulators in their regulation practice. For this reason, also (responsive) regulation has to be considered in its context. This is also recognized in paragraph 3.3.4, and elaborated on further in the next section.

### 3.3.4 Really responsive regulation

With respect to regulating in a context, the theory of responsive regulation, as discussed in paragraph 3.3.3, has limitations. For example, it is not always feasible to enforce by escalating up in the pyramid. In case of the discovery of a potentially catastrophic risk, it might be appropriate to directly resort to higher levels of the pyramid. Also, effectively returning to a lower level in the enforcement pyramid may be hard when the relationship between inspector and inspectee is disturbed (Bruijn & Heuvelhof, 2005). Third critique to the content of the pyramid is that there is a difference between theoretical means and practical means, i.e. a regulator may (for various reasons)

not be capable or dare to use some enforcement measures. If so, these enforcement measures should not be considered in the enforcement pyramid (Baldwin & Black, 2008).

Then, there are two core assumptions of responsive regulation that raise critique (Baldwin & Black, 2008). First, responsive regulation assumes a simple binary relation between inspector and inspectee. Though Ayres and Braithwaite also mention tri-partite arrangements, they do not consider multiple inspectors ('principals') (Ayres & Braithwaite, 1992). The existence of multiple principals can make regulatory regimes significantly more complex as it provides extra opportunities for the inspectee to behave strategically. Second, Baldwin and Black (2008) argue that, opposed to the assumption of Ayres and Braithwaite, behaviour is often not driven by regulatory pressure but by sector culture and forces of competition. Thereby, Baldwin and Black imply the importance of the context of regulation.

Acting upon these limitations, Baldwin and Black argue regulators are to be 'really responsive'. They describe really responsive as follows: 'Regulators have to respond not merely to firms' compliance responses but also to their attitudinal settings; to the broader institutional environment of the regulatory regime; to the different logics of regulatory tools and strategies; to the regime's own performance; and finally to changes in each of these elements' (Baldwin & Black, 2008). Hence, really responsive regulation also recognises the significance of the institutional environment. Although really responsive regulation does not provide a clear framework for the design of a regulatory regime, the acknowledgement of the importance of context and network in itself provides theoretical opportunity for the management of moral hazard.

### **3.4 The institutional context of regulation**

Baldwin and Black (2008) argue that the institutional context is of significance for regulation. This section discusses a way to look at institutions proposed by Williamson in the first paragraph. Element of this context is the existence of multiple principals (regulators/inspectors) and multiple principals (regulatees/inspectees). Starting at paragraph 2, the remainder of this section focuses specifically on this contextual element by studying network (agency) theory.

#### **3.4.1 Studying institutions**

An actor's behaviour is not fully dependent on its relation to the regulator. The interaction between regulator and regulatee takes place in a context that may impose other constraints and opportunities in both formal and informal ways. These 'rules of the game' (i.e. institutions, see appendix II) play an important role in the way actors interact. Williamson (1998) identifies four different levels of institutions based on Neo Institutional Economic (introduced in appendix II) theories. By his categorization, Williamson aims to minimize transaction cost between organizations (Spiller, 2010). However, it may just as well be used to create an overview of institutions and explain their functioning (Koppenjan & Groenewegen, 2005). As such, the Williamson framework (figure 3.5) will be used to evaluate the functioning of the current system.

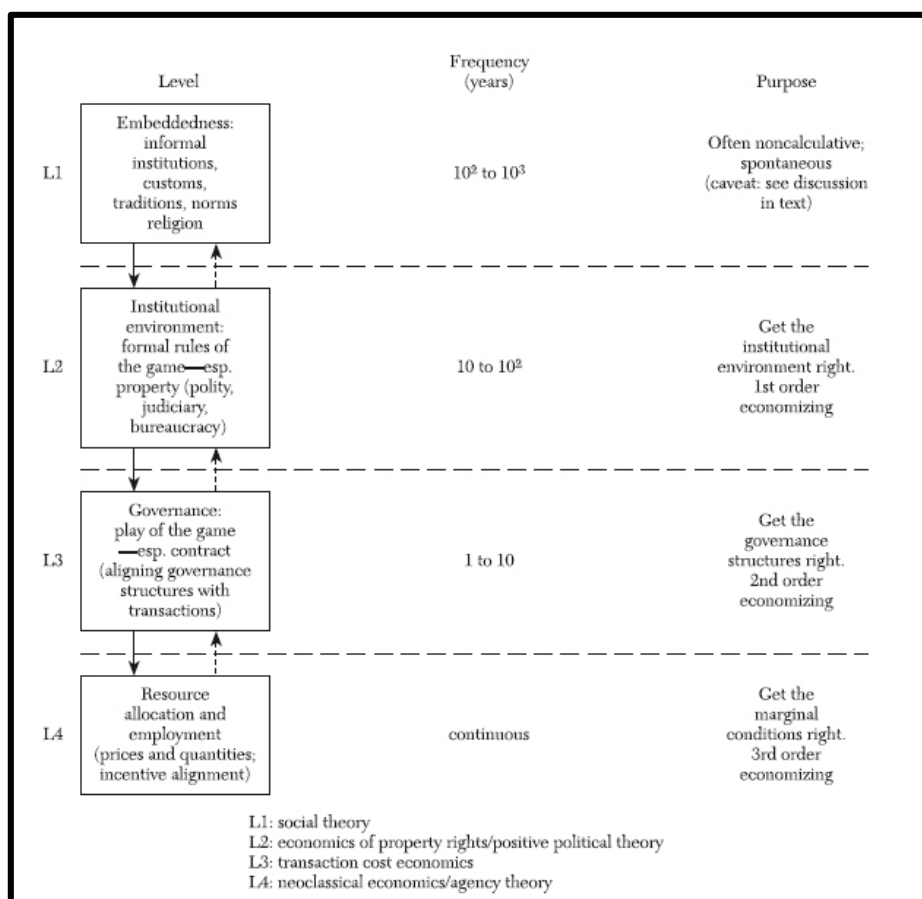


Figure 3.5: Institutional framework of Williamson (1998)

Where the first layer of Williamson focuses on the embedded institutions, like values, norms and attitudes, the second focuses on the formalized institutions like laws. The first two layers together incentivize 'day to day' practice shaped by the third and fourth layer. The third level comprises the formal institutional arrangements, often easier to change than laws. It is this level that comprises, amongst others, many of the regulatory arrangements, e.g. peer monitoring, in place. The fourth and final layer deepens on the interaction between actors in the system. Moral hazard occurs in this layer, but is also incentivized by institutions from the other layers. Note that the layers also mutually influence each other.

In discussing regulation, which can now be related to layer three, it was already hinted on that regulation in practice is mostly no 1-on-1 relationship between a principal and an agent, but multiple principals and multiple agents are existing and operate in a network with other actors. These relationships are categorized in level four and theoretically described in agency theory. Baldwin and Black (2008) argue that the relationships are very important for the functioning of regulation. Considering peer monitoring as a promising regulatory arrangement between agents, the remainder of this section studies the relationship between agents, principals and other network actors.

### 3.4.2 The agency dilemma

The terms 'principal' and 'agent' originate from agency theory (which is founded in new institutional economics, see appendix II). The basis of agency theory lies in the acknowledgement that there is often information asymmetry, uncertainty, and risk (Akerlof, 1970; Arrow, 1971). A dilemma occurs when the two parties are not fully aligned and the agent has more information than the principal

(Eisenhardt, 1989a). The core of a principal-agent relationship is that a party (the agent) is to act in the best interest of another (the principal). Agents will tend to ‘shirk’ when the goals of principal and agent are not aligned (Steenhuisen, 2009). Sharing the precondition of information asymmetry, scholarly literature often considers moral hazard in the context of an agency dilemma, i.e. moral hazard may occur when the agent may benefit from a difference in risk preferences between agent and principal, while negative consequences are for the principal that is not (or cannot be) fully informed. Note, however, that though moral hazard and the agency dilemma might coincide quite often, there is a distinct difference between them.

To make the choices of the agent coincide with the desires of the principal, agency dilemmas are managed through, what literature names, contracts (Eisenhardt, 1989a). Monitoring and using incentives are typical means to make the agent follow the principal’s desires (Stiglitz, 1975; Sappington, 1991). In managing moral hazard, forms of prudential regulation are often proposed mitigation elements of these contracts (see appendix III).

### 3.4.3 Multiple principals, multiple agents

In reality multiple principals (e.g. CFV, WSW) and agents (e.g. corporations) exist. This complication to the single principal-agent relationship makes conflicts between incentives from multiple principals emerging within agents (Waterman & Meier, 1998; Black, 2008). In agency literature, the idea of multiple principals often has a negative connotation and is often associated with information redundancy leading to higher cost (Milward & Provan, 2000). But, as is shown in other disciplines, redundancy in information may also provide opportunities and securities (Torgo, 1993; Wiltschko & Wiltschko, 1994). Though redundancy might increase the cost, but it may also reveal more and better information to the principals, which may be extremely useful when the agent performs complex activities. However, precondition to this advantage is good coordination between the principals (Hawkins, Lake, Nielson, & Tierney, 2006).

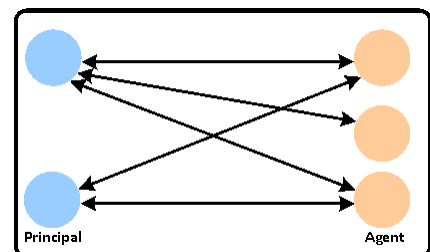


Figure 3.6: Multiple principal multiple agent with bilateral relationships (based on Bruijn & Heuvelhof, 2005)

### 3.4.4 Principals and agents in a network setting

Supervision is not even as simple as a process between principals (i.e. ‘inspectors’) and agents (i.e. ‘inspectees’). In fact, a distinction can be made between a managerial echelon (principal) that is likely to control the inspectors (agents). Simultaneously, the managerial echelon (agent) is controlled again by a political echelon (principal) (Bruijn & Heuvelhof, 2005). As, on each level, various principals may influence various agents, it can be concluded that supervision in fact consists of a chain of multiple principal multiple agent relationships. Note that this chain also continues ‘within’ the inspectee, i.e. the supervised organization. This obviously brings more complexities to effective regulation.

Furthermore, there are all sorts of other organisations (yellow in figure 3.7) that may try to influence the supervision on each level. Think of

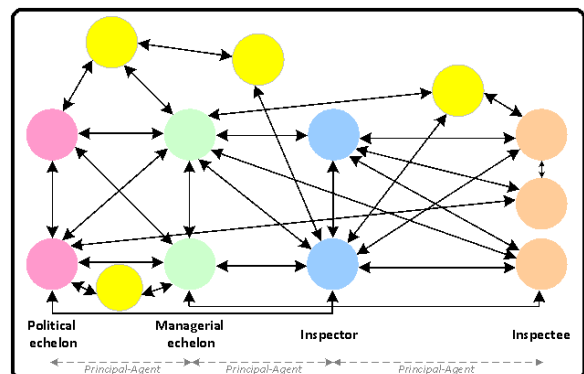


Figure 3.7: Network of principals and agents with bilateral relationships (based on Bruijn & Heuvelhof, 2005)

branch organizations, citizens, media etc. (Hutter, 1997). So, all types of other relations also exist. For example, inspectees might directly contact the political/managerial echelon when they feel that the inspector is not doing its job correctly or might establish these contacts through other organizations, or have 'horizontal' relations (Bruijn & Heuvelhof, 2005).

The network described above is way more complex than the single principal-agent relationship started with. It contains a large number of parties that are mutually dependent and have a large number of relations available to reach their goals (Bruijn & Heuvelhof, 2005). These interdependencies and horizontal relations provide an argument for the functioning of peer monitoring. The horizontal relation between inspectees fulfils a precondition for peer monitoring to effectively manage moral hazard.

However, the multilateral interdependencies also provide an argument against the functioning of peer monitoring as peer decision making is not solely focussed on the regulatory interest. Also, the functioning of the network is dependent on the self-interest, culture and power position of actors in the network (Mukherji, Wright, & Mukherji, 2007). The combination of these factors influence cohesiveness in objectives between actors in the network.

In conclusion, moral hazard and peer monitoring take places in a complex network setting. This network context allows arguments for both the effectiveness and ineffectiveness of peer monitoring in managing moral hazard. The relevance of this context blurs the boundary of this study. For this reason, a case study research design is chosen as it is best capable of working within a relevant context and unclear system boundaries (see section 4.2).

### 3.5 Propositions

So far, this section argued that moral hazard is characterized by separation in ownership, asymmetric information and hidden action. Peer monitoring proves to have potential to limit moral hazard from occurring as peers are argued to have a better information position. As such, peer monitoring arrangements may be an appropriate regulatory arrangement. Effective regulatory arrangements are characterized by a director, a detector and an effector element. However, also the institutional context is significant in the functioning of regulatory arrangements as regulation is embedded in a wider practice. Especially the relations in which regulation is to take place is to be given attention to for the well-functioning of a regulatory arrangement.

To examine the potential of peer monitoring for managing moral hazard, this section develops five propositions used to structure the analysis on the functioning of peer monitoring in the management of moral hazard. Propositions are based on the theory discussed earlier in this chapter. Though many more propositions can be thought of, five is a deliberate choice to limit the extent of the research. Relations between the fields make that not necessarily each proposition needs to be answered to get an impression of the potential of peer monitoring. The propositions presented here were shared, discussed and approved by a peer research group.

	Willingness	Ability
<b>Director</b>	<i>Proposition 1</i>	
<b>Detector</b>		<i>Proposition 2</i>
<b>Effector</b>	<i>Proposition 3</i>	<i>Proposition 4</i>
<b>Responsiveness: Proposition 5</b>		

Figure 3.8: Categorization of propositions

Four propositions are structured through Hood's (2001) elements on effective regulation: director, detector and effector. Furthermore, the distinction in regulation between the willingness and the ability of a regulator to act (Baldwin, Cave, & Lodge, 2012; Bruijn & Heuvelhof, 2005) serves as a basis for the four propositions. The fifth proposition focuses on the (rather normative though scientifically relevant) notion of responsiveness peer monitoring offers in managing moral hazard. The categorization of propositions is schematically represented in figure 3.8. The paragraphs of this section present and discuss the research propositions.

None of the propositions specifically focuses on the role of the peer monitoring context as described in section 3.4. This is because the context is not at the core of peer monitoring as regulatory arrangement. However, the importance of context in the functioning of peer monitoring arrangements was already noticed. The context of peer monitoring plays an important role and special point of attention in discussing the propositions later in this research.

### **3.5.1 Proposition 1: Peers have a sense of urgency to regulate one another**

As peers are accountable for the risk taking behaviour of others, their utility is to some extent dependent on the effort of others (section 3.2). This makes that peers can be classified as principal in a principal agent relationship (section 3.4). Peers differ in their objectives and risk preference. The sharing of risk gives peers an interest in monitoring one another. If peers are willing to shape this idea, they are to start by defining what is acceptable or not, i.e. identify 'directors' (section 3.3).

On the other hand, peers operate in a broader institutional context. Their actions are shaped by regulation and relations with all types of actors in the network. Most, if not all, of these relations are present also present outside the regulatory arena. The context in which peers operate may nuance the suggestion of peers willing to set boundaries on one others performance (section 3.4). Hence, the first proposition discusses the sense of urgency peers have to regulate one another.

### **3.5.2 Proposition 2: Peers have information about each other's behaviour**

Peer monitoring may be especially helpful in the presence of costly information. This insinuates that peers have a) more information and/or b) are better capable to give knowledge to that information (section 3.2). Moral hazard is characterized by asymmetric information and hidden action (section 3.1), making information costly. Based on notions of really responsive regulation (section 3.3), it proved relevant that regulatory drivers are just one of the elements driving (risk taking) behaviour (section 3.4). This institutional context might also hamper the ability of peers to have information on each other's behaviour, i.e. 'detectors'. Hence, the ability of peers to be informed of one others behaviour is examined by the second proposition

### **3.5.3 Proposition 3: Peers may interfere with each other's business**

Subsequent to the first proposition, the third proposition focuses more on the willingness and of peers to sanction each other, i.e. are 'effectors'. The underlying question is whether corporations are actually willing to sanction their peers. As corporations are accountable for one another (section 3.2), it may follow that peer sanctioning is an efficient activity for a corporation to engage in. According to Stiglitz (1990), the idea that peer monitoring may pay off proved important in the effectiveness of peer monitoring. However, peers may not want to damage their relations with each other. Moreover, embeddedness may hamper peers to intervene (section 3.4). Hence, the institutional context might limit the 'effector' willingness of peers. By the third proposition, the willingness of peers to discipline each other is studied.

#### **3.5.4 Proposition 4: Peers have formal and informal means to intervene**

Even when corporations have the necessary information and are willing to set norms and sanction their peers, they still need to have the means. On basis of this proposition, peers have formal and informal means to act, insight is to be created on the ability of corporations to sanction their peers. Regulation theory (section 3.3) proved that not every mean can factually be applied. What mean can or cannot be applied is dependent on the institutional context. It should be noted that this not only entails direct means. Indirect means are just as relevant (section 3.4), e.g. the abilities of a peer to bring a formal external supervisor like CFV to sanction a corporation. In addition, means can either be formally or informally arranged.

#### **3.5.5: Proposition 5: Peers have enough degrees of freedom to adjust regulation to the situation at hand**

The fifth and final proposition is based on the more normative notion of responsiveness. By acting responsive, regulation literature (paragraph 3.3.3 and 3.3.4) argues that the opportunities to achieve compliance are widened. Therefore, peers would need a variety of compliance measures that can be utilized. In addition, peers would need a variety of penalizing measures. By this proposition, attention is given to the extent to which peers are capable to act responsive and apply measures appropriately. Also here, it is both the formal and informal as well as the direct and indirect means that are relevant to consider.



## 4. Case study design

This section introduces the design for the case studies. Section 4.1 to 4.3 discuss what is a case study, why it is appropriate for this study and defines the corresponding semantics used. More on the content, the fourth and fifth section identify the unit of analysis as well as the case study design. The selection of corporations to be studied is done in section 4.6 after which section 4.7 deeper explores the data collection. Section 4.8 describes the way data is analyzed. The chapter concludes with section 4.9 making some preliminary notions on the validity of the case study.

### 4.1 Case study definition

At its very basics, the case study is an approach to explore or describe a phenomenon within its context (Eisenhardt, 1989b). For a long period of time, scholars struggled with the usefulness and position of case studies in scientific research (Gerring, 2004). Abercrombie, Hill and Turner, for example, present the following definition of a case study: “The detailed examination of a single example of a class of phenomena, a case study cannot provide reliable information about the broader class, but it may be useful in the preliminary stages of an investigation since it provides hypotheses, which may be tested systematically with a larger number of cases” (Abercrombie, Hill, & Turner, 1984). Others heavily oppose to this definition, even arguing it is “which if not directly wrong, ... grossly misleading” (Flyvbjerg, 2006). This research follows the definition of Gerring in what a case study is: “An intensive study of a unit for the purpose of understanding a larger class of (similar) units” (Gerring, 2004). A unit is here considered as a bounded phenomenon or instance that is observed in a single point in time or over a delimited period of time.

### 4.2 Appropriateness of case study methodology for this research

Case studies are regarded as a valid method of research for years now. They have mostly been used in ecology, anthropology, psychology and social science. One of their functionalities would be to test the working of scientific theories in the real world (Flyvbjerg, 2006; Baxtern & Jack, 2008). As stated, the use of a case study is a research approach for the exploration or description of a phenomenon. It provides the opportunity to do this using different data sources to reveal and understand different facets of the phenomenon (Baxtern & Jack, 2008). This rather broad description is specified by Yin, who argues a case study design is to be considered when the focus lies on answering a ‘why’ or ‘how’ question in cases where either the boundaries between phenomenon and context are unclear or the contextual conditions are relevant for the phenomenon studied (Yin, 1989).

The main research question of this research is in its essence quite similar to the (more abstract) question of ‘why did peer monitoring not prevent actualities from happening?’. On top, the phenomenon itself is not clear-cut, i.e. risks taken by corporations can manifest themselves in a number of ways, but even more, risk taken are a result from numerous considerations from different perspectives. This also blurs the boundaries between what is context and phenomenon. Hence, the case study is considered a good potential approach following the considerations of Yin.

Related to this, is the fact that case studies provide great opportunity for flexibility. A case study might have unexpected results that take research to new directions. It is this characteristics that also makes case studies less favourable approach (as compared to other methods) for purely (dis)proving a hypothesis (Eisenhardt, 1989b). The topic of this research is hard to capture in strict and formal hypothesis. In fact, the question of this research is more a question of ‘learning’ than of ‘proving’. This makes the flexibility a case study offers favourable and, thus, an advantage.

The drawback of case studies is whether the findings can be generalized to the entire population. As a case study is an ‘intensive study of a unit’, usually a relative small sample is studied (especially compared to more statistical oriented approaches). This brings the risk of studying only the exception(s) of the population (Baxtern & Jack, 2008). Hence, the selection of the sample and cases, as well as the limitations of this selection, are among the most important aspects of the case study design. Furthermore, it is important to realize that the results of a case study by its own cannot be generalized to the whole population automatically, but will most likely require further research (Eisenhardt, 1989b). Taking notice of these drawbacks, the case study still appears an appropriate research method for the relatively unstructured and contemporary case of peer-to-peer arrangements in the Dutch social housing sector.

### 4.3 Semantics

As Gerring is already followed in his definition of a case study (‘intensive study of a unit for the purpose of understanding a larger class of (similar) units’), Gerring is also followed in his further description of case study semantics. A ‘population’ (Dutch housing corporations) is comprised of a ‘sample’ (what would then be a subset of corporations studied) as well as corporations that are not studied. Within the sample, ‘units’ (e.g. the working of peer-to-peer arrangements) are studied at moment in time, i.e. ‘cases’. Cases are built up on a number of dimensions, i.e. ‘variables’. The state of a variable is based on ‘observations’ (Gerring, 2004). Hence, the terms of population, sample, unit, case and observation are nested in each other. A schematic representation of the relation between the terms observation, variable, case and unit is shown in figure 4.1.

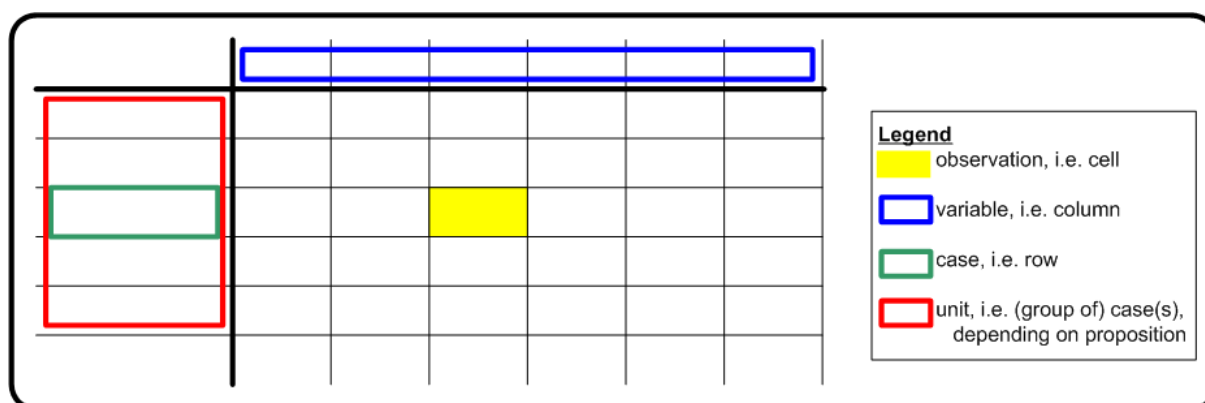


Figure 4.1: Schematic rectangular representation of the relation between semantics (observation, variable, case and unit)

### 4.4 Unit of analysis

Miles and Huberman are followed in their definition of the unit: “a phenomenon of some sort occurring in a bounded context” (Miles & Huberman, 1994). By this research the effect of the institutional context on the working of peer-to-peer arrangements in managing moral hazard in the Dutch social housing sector is explored. The main interest of this research lies in, i.e. the unit of analysis is, the peer-to-peer arrangements. The other elements, i.e. the ‘effect of institutional context’ and ‘moral hazard in Dutch social housing sector’, are more important for scoping and delineating the case study.

### 4.5 Type of case study

Three types of case studies can be distinguished: descriptive, exploratory and explanatory (Yin, 1989). In a descriptive case study, the phenomenon is described in the real life context in which it

occurs/occurred. The exploratory type is used when those situations are studied in which the phenomenon has no clear outcome. The explanatory case study is used for explaining presumed causal relations of phenomena that are too complex for a survey or more experimental strategy (Baxtern & Jack, 2008). As the objective of this study is more than purely descriptive, but not as much as explaining causal relationship on the working of peer-to-peer arrangements, it comes as no surprise the type of case study done in this research is categorized as exploratory. More operationally, the objective of the case study is to gain understanding in (combinations of) institutional elements that play a role in the functioning of peer-to-peer arrangements in the Dutch social housing sector. As such, the exploratory type seems most appropriate.

The following decision to be made is that on type of case study design. As there was already chosen for a single unit (i.e. holistic design), basically, a decision has to be made on the sample size, i.e. should a single corporation or multiple corporations be studied to gain the best understanding of peer-to-peer arrangements? The answer to this question lies in the role of the case study in this research: providing insight into an issue. As such, the case study is of secondary interest and plays a supportive role to facilitate our understanding of the practical working of peer-to-peer arrangements. Stake classifies this types of case studies as 'instrumental' (Stake, 1995). Therefore, it would be nice if the results of the case study could, to some extent, be seen as typical for the population of corporations. From this, it follows that multiple corporations will be studied (i.e. a comparative design) that will have to be carefully selected. This is done in the next section.

#### 4.6 Case selection

The selection of the samples is a trade-off between sample size and depth of study, as the resources of this research are limited. It was already argued that multiple corporations are to be included. It is chosen to further limit the amount of corporations as much as possible, to be able to study in a much detail as possible given the resources of this research. Therefore, three corporations will be studied. Obvious downside of this choice is that it limits the generic power the research.

There are a number of axioms that can help us select 3 corporations out of all 389 corporations in the Netherlands. The first is size, the financial performance and third is the activeness of a corporation. In social housing, size is a really ambiguous concept. Size can be considered as the social capital of a corporation that is has to preserve by law ('BMV', see appendix I for abbreviations). BMV, however, is a number that can be based on different equity concepts that have significant influence. For example, based on the corporate values (Dutch: 'Bedrijfswaarde') (currently mainly used by CFV), the sector holds €31 billion of equity, while this is €179 billion based on the market values and even €300 billion based on the vacant value (Dutch: 'leegwaarde') (Burger, 2012). Before ending up in a deep discussion on what measure to use best, it here suffices to use a way simpler measure for size: number of housing unit, i.e. vhe. Considering an average corporation has 6200 vhe, a distinction is made between large and small corporations. The size of a corporation is also an indicator for the risk carried by other corporations, i.e. the size of peer-to-peer consequences, and may therefore be considered a factor for the 'peer-to-peer incentives'. Therefore, two larger corporations and one smaller corporations are studied.

The financial performance is, again, an ambiguous concept. It can be measured in terms of the (leakage of) social capital, but also by solvability. What the axiom represents though, is the financial

problems of a corporation. In the case study, two corporations in financial trouble will be examined and one corporation that is doing (relatively) well.

Third, corporations can be categorized on their activeness. Some corporations tend to undertake more activities than others. The focus of this research lies in corporations that actively engage in projects. Hence, it is chosen to only select corporations that are relatively active (as well as the actors surrounding them) and make use of the manoeuvre they gained by the financial autonomization. Note this does not necessarily mean only corporations in so-called growth regions are included. As is shown later, also corporations in so-called contraction regions are topic of study. This decision limits the generalizability of the case study. It is, however, considered necessary because of the small sample size and available resources.

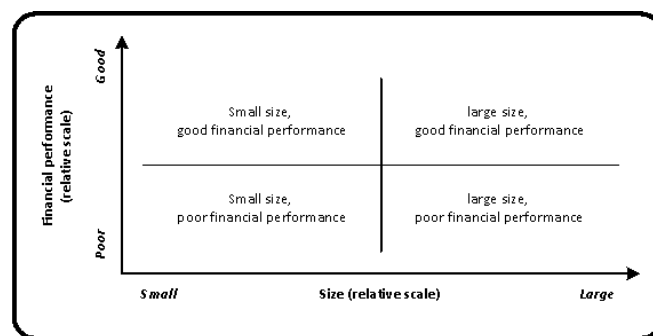


Figure 4.2: Schematic categorization of (active) corporations

In summary, three relatively active corporations are studied. Two of three corporations belong to the larger group and two of the three corporations are in financial problems. A schematic representation of the sample categorization is given in figure 4.2. From this, it follows there are two possibilities for search of three corporations. First option is to study two corporations that are relatively large and are in relative large financial problems and a third smaller corporation that is not in financial problems. As of both categories the third corporation has more of a 'benchmark function', it makes no sense to study a smaller corporation that is financially performing (relatively) well. Therefore, the second possibility is more desired:

1. A relatively large corporation with a relatively poor financial performance
2. A relatively large corporation with a relatively good financial performance
3. A relatively small corporation with relatively poor financial performance

In each category, multiple corporations can be thought of. The decision on specific corporations that are included is therefore based on the availability of information. On this basis, it is chosen to study WSG (a relatively small corporation in the western of the Noord-Brabant province) and Servatius (a relatively larger corporation in the south of the Limburg province). Both corporations received financial restructuring support of CFV. Based on CFV experience, the third, larger corporations with a relative good financial performance that actively acts in an active environment is chosen to be 'Woningstichting Eigen Haard' (active in the city and region of Amsterdam). Profiles of the corporations are found in appendix X (Servatius), appendix XI (Eigen Haard) and appendix XII (WSG). Figure 4.3 gives an overview of the sample selection.

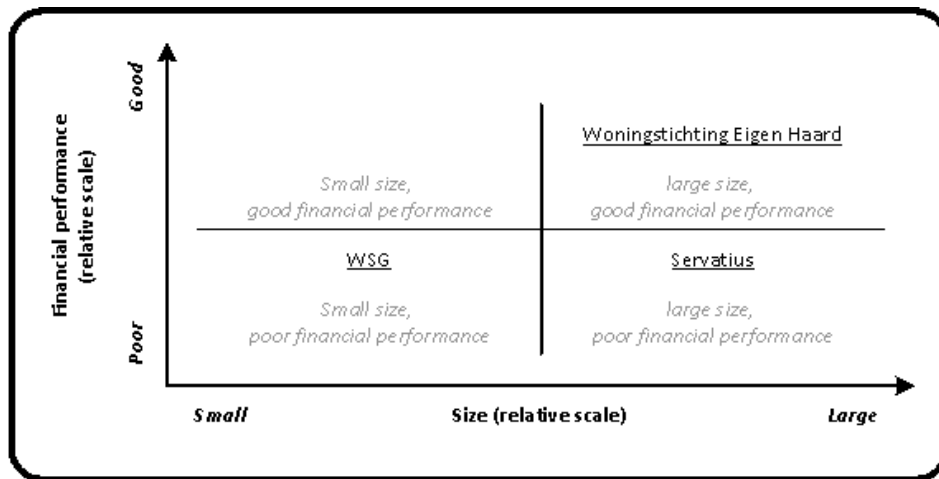


Figure 4.3: Schematic categorization of sample corporations

What is important to realize, is that these corporations operate in different regions of the Netherlands (figure 4.5) and are subject to different demographic developments (figure 4.4). Where Servatius operates in a region with a declining population, Eigen Haard operates in a region with a growing population. WSG finds itself somewhere in between (PBL, 2010).

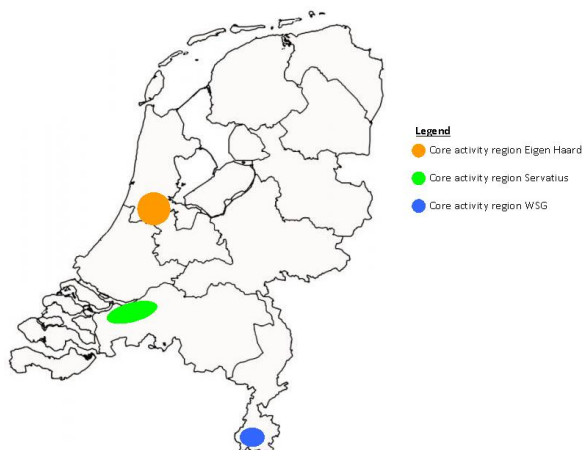


Figure 4.5: Geographic positioning of studied corporations

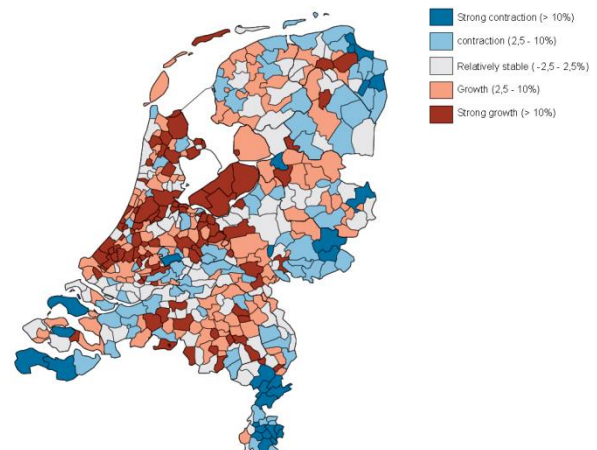


Figure 4.4: Population developments 2008-2040 (adapted from PBL, 2010)

## 4.7 Data collection

In this case study, three different types of sources of information are used: documentation, archival records and interviews. For the quality of the analysis Yin argues it is important that 1) multiple sources (either inter or intra data type) are used as evidence on a finding as much as possible, and 2) there is a clear 'chain of evidence'. The latter meaning that there should be a clear link between questions asked, data collected and conclusions drawn (Yin, 1989). It is also for this reason that the approach of 'pattern-matching' is used for linking data to the propositions, i.e. to do the analysis.

As the unit of analysis is the peer-to-peer arrangements of corporations. As there are formal 'external' supervisors, i.e. CFV/WSW/BZK, the working of peer-to-peer arrangements may well work through CFV. It may also work through WSW and BZK, but as more information is available for CFV, and CFV is the official external financial supervisor, it is chosen to focus on CFV. For each case, it is attempted to get information from mainly three sources: CFV, a corporation, and 'a peer'. Corporation act in a (system) context, that is also relevant for the way peer-to-peer arrangements (and the regulator) function. This is schematically represented in figure 4.6. News articles and earlier interviews may act as a complementing source of information.

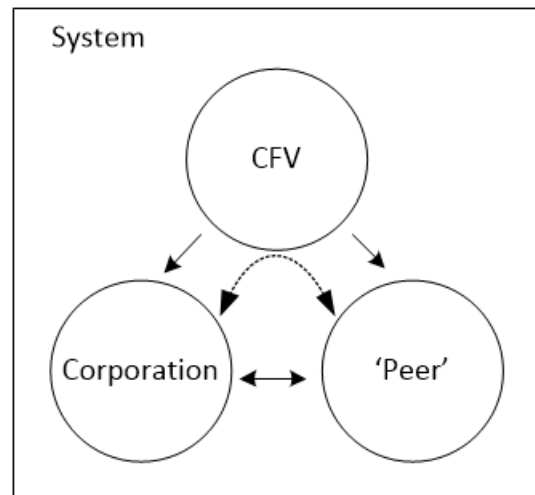


Figure 4.6: schematic representation of potential ways of working of peer to peer arrangements in a system.

### 4.7.1 Documents and archival records

Moral hazard is a topic not commonly studied in social housing. Neither is peer monitoring a topic commonly studied in social housing. This makes evidence finding in publically accessible documents and archives hard. For this study, it is potentially very beneficial to have access to any (written) communication between peers. However, this is not possible for this study in its current set up.

Nevertheless, publically accessible documents may contribute in context setting and finding underlying argumentation. For that reason, for each corporation of study, the following documents and archives are used:

- Annual reports of the corporation over the financial years 2008-2011
- CFV CiP analysis of the corporation over the financial years 2008-2011 (except WSG)
- CFV CiP analysis of the corporation peers in the regional reference group over the financial years 2008-2011
- BZK assessment letters of the corporation over the financial years 2008-2010

Apart from this documents, a variety of documents is studied on the basis of preliminary case study results specific to the corporation of study. An example is documentation concerning the Fountainhead project and 'new kit' project of Eigen Haard.

## 4.7.2 Interviews

*Confidential*



## 4.8 Data Analysis

Two strategies are distinguished for the collection of data. First is the development of a framework for that analysis of collected data. Second is the usage of propositions. This study uses the latter strategy, thereby using the following propositions (as they are described in section 3.5):

- Peers have a sense of urgency to regulate one another
- Peers have information about each other's behavior
- Peers may interfere with each other's business
- Peers have formal and informal means to intervene
- Peers have enough degrees of freedom to adjust regulation to the situation at hand

## 4.9 Validity

For performing case studies, four criteria are relevant to consider for the quality of the research: construct validity, internal validity, external validity and reliability (Yin, 1989). Internal validity is only relevant for explanatory case studies. Hence, it is not discussed here. The three remaining criteria are briefly discussed in this section.


Construct validity focusses on the correct establishment of operational measures for the concepts of study. Therefore, specific type of changes are to be selected. In this case study, this is done by the propositions discussed in section 3.5. To increase the construct validity, Yin (1989) identifies three tactics: the use of multiple sources of evidence, establishment of a chain of evidence and a report review by key informants. In this research, these tactics are respected by having multiple interviews with different people in different organizations (i.e. CFV/corporation/peer) for each case. These interviews are also complemented by written documents and an institutional analysis performed in chapter 5. Furthermore, multiple corporations are studied (as discussed in section 4.4). The findings of the analysis performed will be discussed with the involved DAs of CFV in order to respect the third tactic.

External validity deals with the issue of knowing whether case study findings are (analytically) generalizable beyond the studied cases. This issue is closely related to the amount of replications. As a start, this research uses a multiple-case design, thereby contributing to the external validity. The external validity is improved by studying more cases and replications of this study (on other cases).

Reliability concerns whether the same results are produced if the same procedures are followed. Reliability is, to some extent, comparable to external validity but emphasizes on doing the same case over again, in contrast to external validity that discusses replications on other cases. Two elements contribute to the reliability of a case study (Yin, 1989). First, the use of a case study protocol. Conceptually, the protocol is discussed already in section 3.5, 4.7 and 4.8. The second element concerns the development of a case study data base, i.e. (an overview of) the evidentiary base on which the findings are based. This evidentiary base is established through in text referencing. The interviews are found in appendices XIII and XIV.

In general, it is important to notice that the validity is not 'sufficient' or 'insufficient'. Instead, validity is more a factor that provides arguments for 'trust' in the findings of the research. As such, validity can always be better. In this research, as in many researches, the most important limitation to the validity is the availability of means (mostly time in this case).





## Part II – Analysis

## 5. Institutional analysis

This chapter provides an institutional analysis of corporation financial risk taking in the Dutch social housing sector. In doing so, the structure of this chapter is similar to that of the literature analysis (figure 5.1). The first section deepens on the opportunities and motivations of corporations to engage in risk taking and show their moral hazard behavior. The institutional arrangements regarding peer monitoring are discussed in the second section. The third section places this primary relation in the context of other regulation in place. Further context is elaborated on in the fourth section. Each section will conclude with notions on the propositions. The chapter will conclude with findings on the propositions.

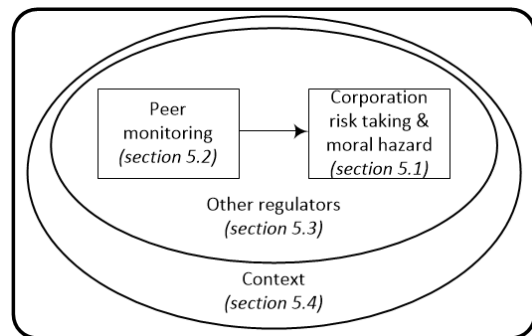


Figure 5.1: Structure of institutional analysis chapter

### 5.1 Moral hazard in the Dutch social housing sector

In this section, an overview is given on the corporation possibilities to engage in risk taking and moral hazard behavior. The first paragraph argues on how and why corporations may take on risk. The second paragraph deepens on the opportunities of corporations to engage in risk in the second paragraph. The third paragraph relates this to the presence of moral hazard in the sector. Positive elements of this moral hazard are discussed in the fourth paragraph, before concluding with some notions on the propositions in the fifth paragraph.

#### 5.1.1 Corporations are entrepreneurs with social goals

Corporations in the Netherlands originated in the cities where rich employers organized housing for their employees to improve living conditions. Corporations significantly grew during rebuilding the Netherlands after the Second World War. By this time, corporations acted as dedicated bodies of municipalities in developing neighborhoods (Hoekstra, Hoogduin, & Schaar, 2012). Providing housing for the weaker of society, the position of corporations further strengthened when the right for housing was included in the Dutch constitution (Rijksoverheid, n.d.d.).

In the early 1990s, both the organizational and financial ties between corporations and municipalities were cut (although corporation loans are still guaranteed by the national government and municipalities) (appendix VI). Being private organizations, however at the same time having a public goal as their statutory reason of existence, corporations are classified as social enterprises (Dutch: 'Maatschappelijke ondernemingen') (appendix VII). The status of social enterprise makes that corporations have no clear owners and can't do any dividend payments. As a consequence, corporations don't experience real pressure on return of investments (Hoekstra, Hoogduin, & Schaar, 2012). This, in combination with strong equity positions also limits the incentives for good risk management.

In this hybrid structure, an attempt has been made to combine the best of both worlds. Autonomous organizations experience market opportunities and can use their expertise for the effective and efficient allocation of their resources, while the government is able to set the context in which corporations may operate and have the responsibility on realizing their social goals (Priemus, 2003). However, this hybrid structure carries two core risks that are best explained in their extremes. The first risk is that, corporation may be so independent, the government has no significant influence and, therefore, the responsibility of the minister is no more than phantasm. The second risk is that corporations are protected from the market to such an extent that they don't get (sufficient) incentives for effective and efficient allocation of their resources (appendix VII).

In practice, these two competing risks create a 'bandwidth' of corporation cultures. In fact, a transition is occurring from the traditional public dedicated bodies to private market organizations serving a public goal. It is interesting that, over the entire scale, financial wealth and growth generally is not the highest objective. This is mainly so as 1) corporations have no owner demanding market efficiency and returns, and 2) it is prevented by law to extract financial means of a corporation (appendix VII). In both cases the objective of corporations therefore focuses on real estate. In the 'market culture', this means prestige is considered more in terms of pluriformity in activities and growth in housing unit volumes. Falling in between the public and private sector, corporations prove to be competitive, but are no real competitors (appendix VI).

Regardless of the corporation culture, the autonomization of corporations made corporation entrepreneurs with a loss giving core objective (Bulter, Dalen, Eiffinger, Koedijk, Teulings, & Witteloostuijn, 2006). It is for this reason, corporations are also allowed to sell their property. The loss giving core objective is also one of the primary reasons why corporations are more and more allowed to engage in commercial activities over time (appendix VII). With their public capital heritage (and corresponding strong equity positions), and loans guaranteed by government, the engagement of corporations in commercial activities raises quite some critique. For this reason (and European regulation concerning state aid), the guaranteed loans are now subject to strict norms and can only be spent on a limited number of activities.

In conclusion to this paragraph, corporations have to be entrepreneurs and take risk since their financial autonomization. Not operating in a real competitive market, corporations are competitive to each other but not real competitors as they are missing market sanctioning mechanisms. As the core of corporations is loss giving, corporations are allowed to sell their equity and engage in commercial activities though this increases the risk for corporations. The hybrid sector structure creates lower incentives for corporations to work efficiently, as corporations are placed in between markets and governments.

### **5.1.2 Opportunities of corporations to engage in risk**

The activities corporations may engage in are described in a ministerial decree referred to as BBSH (appendix VII). However, the activities are not clearly demarcated and leave room for interpretation. For this reason, approval of the Ministry of the Interior (BZK) is often asked by a corporation for new activities. Over the years, also BZK proved not to allow corporations to use the leverage the BBSH offers. In this way, BZK also approved the Campus project of Servatius and the SS Rotterdam project of Woonbron.



Also, because of the financial security structures, corporations are capable to finance projects largely through loan capital. Many business investments are partly financed through loans. However, financiers always require investors to invest a certain share of their own capital. Because of the guarantees of the financial security structure, financiers are relatively sure their loan will be repaid. This makes them willing to finance larger shares of projects but makes them also care less on the total loan pressure of a corporation. Also, the financial security structure lowers the interest to be paid on loans, thereby creating extra leverage on the financial position of corporations.

Third, since 2007, loans are guaranteed using facilitation volumes (appendix VIII). On the basis of pledge and expected cash flows, WSW determines the amount of financing it guarantees. This enables corporations to have access to financing, even when not directly used for investments. This creates extra room for leverage. This way, financing has been used for liquidity purposes (e.g. fulfilling margin calls or temporarily finance commercial activities) because of a lack of supervision on the spending of money (Hoekstra, Hoogduin, & Schaar, 2012). This is also supported by complex techniques to create extra financing opportunities. Some well-known techniques are 'slepen' and the use of subsidiaries. These are further explained in appendix XIII.

In conclusion to this paragraph, corporations have many opportunities to take on risk. Although formally limited by European and Dutch regulation, corporations are factually able, and practically allowed, to engage in many activities. They are also attract high amounts of cheap loans through the security structures. The usage of these loans is not fully monitored, creating many freedoms for its usage.

### **5.1.3 Moral hazard: Corporations are entrepreneurs that keep benefits, but share risk**

Corporations financially contribute to each other in case of financial problems (appendix VIII). By doing so, the incentive to be careful with risk is reduced even more (Blokland, 2013), i.e. incentivizing moral hazard. It is in this context that often the investment in commercial activities is not really profitable and sometimes loss giving (Gruis, 2013). Based on the above mentioned findings, starting point of this research is that moral hazard is indeed existing in the Dutch social housing sector. In this research, moral hazard is defined as 'strategic behaviour of an actor, from which the positive effects of risk taking are for the actor itself, while the negative effects are (partly) for others'. Proving the existence of moral hazard is extremely hard due to its specific characteristics (chapter 3). Still, this chapter indicates moral hazard is present in the Dutch social housing sector based on writings of industry thought leaders.

Rochdale, SGBB, Woonbron, WSG, Servatius and obviously Vestia, all are Dutch corporations that faced scandals over the recent years (Financieel Dagblad, 2012). Laurentius, De Key, Stadgenoot, Ymere, Portaal, Wooninvest, Stichting Woningbouw Slochteren, 't Heem, Goed Wonen, Wooninvesteringsfonds, Zaandamse Volkshuisvesting, Algemene Woningbouwvereniging Monnickendam, Kennemerhave and Veron, are fourteen corporations that currently are under intensified supervision by the financial regulator of the sector CFV (Ministerie van Binnenlandse Zaken en Koninkrijksrelaties, 2013a).

The allowance to engage in commercial activities made a number of corporations compare themselves to commercial real estate agencies more than other corporations (Koolma, 2013; Priemus, 2013). Not facing any requirements on return of investments and being able to attract cheap financing because of risk sharing over corporations with backing of governments, corporations

actively engaged in, amongst others, university campuses, a historic steamship, and even prostitute housing (Calon, 2013). None of these activities was or is strictly illegal for a corporation to engage in. Still, the excess of activity in (commercial) activities of some corporations does not directly seem to add to the corporation's public goal.

Though hard to prove for each individual case, multiple leading authors from the Dutch social housing sector argue the risks taken are, amongst others, explained by the cheap financing and corresponding sector security structures (Blokland, 2013; Calon, Het kan beter, 2013; Schaar, 2003). The consequence of these security structures is that, in the event of risks materializing, negative consequences are shared by all corporations. For example, housing corporations have to come up with €700 million (almost €300 per housing unit) for the financial restructuring of Vestia. Hence, moral hazard appears to play an important role in contemporary issues in the Dutch social housing sector.

#### **5.1.4 Managing moral hazard: protecting positive elements of risk sharing**

The risk sharing between corporations also has positive elements. First and foremost, the sharing of risk over corporations and further backing by governments make that corporations cannot go bankrupt. Hence, the security structures protect the tenants of social housing homes. Secondly, the cheap financing opportunities of corporations is a direct consequence of the financial security structures. For tenants, this cheap financing may bring an advantage of up to €35 per housing unit per month (Hoekstra, Hoogduin, & Schaar, 2012). A third element resulting from the security structures is that the guarantees allow corporations to finance their projects with a relative large share of loan capital in comparison to regular business. This makes it possible that healthy corporations may have two thirds of their total balance sheet financed through debts. This is the most influential consequence in terms of business operations as it long enabled the activity of corporations.

For this research, managing moral hazard is considered the prevention of the potential negative consequences of risk sharing elaborated on in the previous paragraph, while protecting the strengths identified in this paragraph. The next paragraph deepens on the opportunities of corporations to take on risk, i.e. influence the chance of the negative consequences of risk sharing materializing. The focus of regulation (and, hence, also peer monitoring) is on preventing negative consequences of moral hazard. This study therefore only refers to the positive elements of moral hazard when regulatory activities (from peers or others) limits the strengths of moral hazard.

#### **5.1.5 Preliminary notions for the propositions**

Section 5.1 does not directly focus on peer monitoring functioning in managing moral hazard, but on the moral hazard itself. However, still something is to be said on the propositions based on the willingness of peers to monitor one another (proposition 1 and proposition 3). The financial security structure, along with context issues, gives corporations many freedoms to engage in risks. Peers are accountable for the losses of each other when risks materialize. This provides a sense of urgency for peers to regulate one another and, therefore, to discuss what is acceptable and what is not. It also provides an incentive for peers to intervene at each other when they feel others take on too much risk. Though negative consequences of risk taking should be mitigated, the strengths should be protected.



## 5.2 Peer monitoring

Based on the moral hazard discussed in the previous section, it is made clear that peers have incentives to regulate one another. This section further studies how peer monitoring is institutionalized in the Dutch social housing sector. As such, this section distinguishes between 1) the willingness and 2) the ability of peers to monitor one another. The third paragraph reflects on this section by providing preliminary notions on the propositions.

### 5.2.1 Willingness of peers

On the financial domain, peers have incentives to monitor each other mainly by the financial security structures. WSW, the guarantor of loans (over €86 billion in total), has a risk equity of €485 million directly filled by corporation contribution (Appendix IX). As a second layer, WSW is able to claim an extra €3,2 billion of corporations through a so called outstanding reserve (Dutch: 'obligo reserve') (appendix VIII). Also the financial regulator, CFV, has a fund that may be used for the financial restructuring of corporations. Also CFV is capable to oblige extra contributions of corporations for the financial restructuring of others (appendix VII). Before the Vestia case, the maximum extra contribution was set to 1% of the total yearly revenues from rents. Since Vestia, this has been increased to 5% (appendix VIII). In practice, this means a corporation might have to contribute tens of millions of euros for the saving of other corporations (Plaisier, 2013), without potential of reward by these risks. Hence, there is a strong incentive for peers to regulate one another and intervene when necessary.

### 5.2.2 Ability of peers

The ability of peers to regulate is discussed by the regulatory elements identified in section 3.4: Director, detector and effector. No proposition has been formulated on the ability of peers on the director element. Still, having norms (i.e. director) is precondition to be able to sanction as norms state what is acceptable and what is not. Hence, it is still relevant to discuss the director element here.

#### *Director*

Corporations are united mainly in two ways: regionally and nationally. An example is the Amsterdam federation of corporations (AFWC). These groups represent the combined corporations of the region to governments on the various levels and are used as discussion groups to adjust regional housing policies (AFWC, 2013). It appears these regional groups don't directly contribute to peer regulation. It also appears these regional gatherings mostly exist in the more urban/city areas.

Nationally, corporations are gathered by branch organization Aedes. About 95% of the corporations is member of Aedes. Through Aedes, the corporations established norms on the field of governance and risk management in the so-called governance code (Aedes, 2012a). The governance code is an attempt to improve the quality of internal supervision. As such, it provides a set of principles on the topics of compliance, the nomination of the executive board and supervisory board and on audit functions. Each principle is also made explicit through multiple specific provisions. The code contains no hard norms on financial performance. However, multiple provisions aim to ensure good financial information quality for two purposes: accountability (in the governance perspective) and risk taking quality (in the commercial perspective). A corporation is not bound to comply with every provision of the code. Only some provisions are compulsory, one of which is that a corporation should let itself get audited at least once every four years, by a SVWN approved organization (appendix VIII).

SVWN is the organization that arranges the content and procedures on audits and appoints organizations that are allowed to perform the audits (appendix IX). The audit will result in a number of recommendations to the corporation, amongst others on their financial position and the organization of the internal checks and balances on risk taking (appendix VIII). The SVWN norms are to be seen as a representation of the norms considered by the combined Dutch corporations.

Within Aedes, subgroups of corporations exist (called 'kringen') of which corporations may proactively become member of. These groups are formed on a specific topic, e.g. derivatives. Hence, a corporation may be part of different subgroups (appendix IX). However, the role of these groups focusses more on learning of each other than regulating on each other (Dreimüller & Van Engeldorp Gastelaars, 2008).

In conclusion, peers meet in a variety of gatherings. However, the national Aedes organization seems the only effective form in where peers may set standards for one another. This is currently done through the governance code. Peer meetings are mostly informative and have no regulating objective.

#### *Detector*

There is no formalized system from which peers are able to request data on one another. Still, this does not mean peers don't have information on one another. They share information in a number of different ways. First, the corporation world is relatively small (Haffner, Elsinga, & Wolters, 2005) and most corporations operate in geographically distinct areas (appendix VII). This makes that corporation board members know each other personally and they have knowledge on the ambitions of one another. This ability may be stronger for corporations that are active in regional gatherings as peers than encounter each other more often.

In these gatherings and from local media, peers also gain knowledge of the activities of one another, most specifically on the 'crown-jewels' of each other (Hellinga, 2005). For the financial performance, this is somewhat different. Peers are competitive to each other and therefore financial information is strategically valuable (appendix VI). However, output of Aedes and SVWN findings is publically accessible (appendix IX). These findings provide corporations with some general notions on their peer performances. Still, peers have no detailed insights in the financial performance of other corporations, nor in the buffering capacities for planned future activities.

In conclusion, it appears the ability for peers to gather data is limited. With no formal systems in place for peers to request data of one another, peers are best able to gain knowledge on the ambitions and activities from one another in the informal network through the regional networks. Competitiveness also hampers information sharing, especially financial information. Aedes and SVWN findings, however, provide peers with some preliminary notions on this field.

#### *Effector*

Peers are able to sanction their peers through Aedes and, indirectly, through SVWN. Obviously, peers may approach each other in an informal way. However, effect of these 'threats' is doubtful without the backing of real disciplining mechanisms.

When a corporation deviates from the sector code it should do so with the explicit approval of the supervisory board and explain this decision in its annual report. When a corporation does not act to the AEDES principals, a corporation can be excluded from membership. This, for example, happened

to Vestia (Hoekstra, Hoogduin, & Schaar, 2012), though officially Vestia withdrew the membership itself (Vestia, 2005). In fact, this measure is not effective as it isolates a corporation from its peers. Though it is the most stringent measure that AEDES can take. Formally, the internal Aedes organization provides a judgment on compliance of the Aedes principles (appendix IX). However, corporations are closely involved through Aedes meetings (Aartsen, Keet, & Peij, 2006).

As already discussed only a limited number of provisions is compulsory, one of which is that a corporation should let itself get audited at least once every four years, by a SVWN approved organization (appendix VIII). The audit results in recommendations or warnings for corporations on fields it should better focus on. Peers are not involved in the recommendations. Figure 5.2 gives an overview of measures supported by peers. As can be seen, there are no 'in-between mechanisms'. If the relatively softer arrangements do not achieve compliance, peers themselves only have an 'ultimate' measure available.

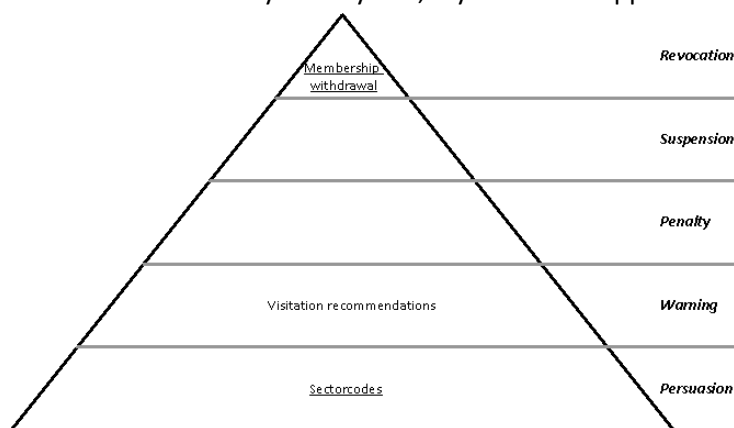


Figure 5.2: Schematic categorization of sanctioning arrangements (underlined arrangements are considered peer monitoring)

In conclusion, the ability for peers to act as effector is fairly limited. The sector codes established by peers through Aedes aims to persuade corporations to comply. In case of non-compliance, peers only have limited possibilities to intervene, other than to withdraw the membership of the respective peer. By means of the audit recommendations, corporations are warned on topics that are to be improved by the corporation. However, even though peers obliged the audit to one another, they are not involved in the further sanctioning mechanism.

### 5.2.3 Notions for the propositions

The financial security is a strong incentive for peers to regulate one another. At stake for the combined peers is a contribution up to 5% of their total annual renting revenues yearly next to an outstanding reserve of €3.2 billion. The ability of peers to regulate one another lays in the corporation gatherings in the region and nationally (through Aedes). It is in these meetings peers make agreements on standards and get some notion on the activities and ambitions of others. As peers are also competitive, they limit the sharing of financial information in this respect. When it comes to sanctioning, peers are dependent on Aedes. Sector codes are in place to persuade compliance, but in case of non-compliance, a corporation can basically only lose its membership. A specific implication of the sector code is the audit of corporations by a SVWN approved organization. However, peers are not involved in both the execution of the audit as well as its recommendations.

## 5.3 Regulatory context of peer monitoring in the sector

The Dutch social housing sector is not designed on peers monitoring one another, although self-regulation was a value long strived for (Aedes, 2012a). Instead, formal regulators are assigned to regulate corporations. This section studies how these regulators influence peer monitoring in the Dutch social housing sector. This section distinguishes between 1) the willingness and 2) the ability of peers to monitor one another. The third paragraph provides notion on the propositions.

### 5.3.1 Other regulators influencing the willingness

As from 2010, the DG housing (Dutch: 'Directoraat-generaal Wonen, Bouwen en Integratie') is under the responsibility of BZK. Before 2010, the DG housing performed similar tasks but under the responsibility of the ministry of VROM. Regulation of BZK focusses on the legitimacy, governance and integrity of corporations as well as their social housing performance (appendix IX). Although the regulation fields of BZK are quite clear, there are no clear norms that structure the regulation activities of the department (Hoekstra, Hoogduin, & Schaar, 2012).

By law, CFV is assigned as the formal regulator on the financial performance of corporations. As such, CFV regulation focusses on the solvability and continuity position of corporations (appendix IX). Each year, CFV publishes so-called policy rules in the Dutch government gazette. The rules elaborate on the fields of attention in their regulation (appendix VIII). Currently, six fields are distinguished: quality of information, maintaining social capital (BMV), risk management, liquidity, solvability and continuity (appendix IX). Each field is operationalized by multiple ratios and criteria of interest, including common accounting concepts as ICR and DSCR. The exact norms used for a corporation are confidential for corporations (appendix VIII).

Through WSW, housing corporations are able to borrow money at favourable interests by providing guarantees to the financiers (Appendix IX). The objective of WSW is twofold: First, WSW aims to act as an optimal financier towards corporations; second, they act as a bank, making the repayment of loans a core activity (appendix VIII). This makes the activity of WSW overlap that of CFV to some extent, especially in the field of (financial) risk management. However, there are two fundamental differences between the CFV and WSW. First, CFV is a formally appointed regulator, where WSW is a private initiative for arranging cheap sector financing. As such, WSW is less a regulator. However, the importance of the core activities of WSW makes it function (appendix VIII) and being recognized as a regulator (appendix IX). The second fundamental difference sprouts from the objective of WSW. As WSW is mainly interested in the repayment of loans, they are mainly interested in the corporation's cash flow predictions (supported by equity positions for example). CFV, focusses on solvability and continuity, and is mainly interested in the equity positions (supported by cash flow predictions).

In conclusion, the existence of three regulators, whereof two are focussing on the financial situation of a corporation including risk taking, makes the sector relatively heavily regulated (Hoekstra, Hoogduin, & Schaar, 2012). This reduces the sense of urgency for corporations to regulate one another. Speculative, it also might make it less tolerated for peers to intervene at one another.

### 5.3.2 Other regulators influencing the ability

The ability of peers to regulate is again discussed by the regulatory elements identified in section 3.4: Director, detector and effector.

#### *Director*

Each of the regulators works on its own way. BZK, regulating on legitimacy, integrity, governance and social housing performance is for its norms relatively bound to regulation. In case of doubts, BZK takes its decisions on an individual basis. This most often considers individual projects over a variety of different axioms. Setting norms for what is acceptable for corporations to engage in is relatively heavily influenced by politics (appendix IX).

For CFV and WSW this is slightly different. Both set their own norms and methodologies and are free to do so. WSW, being a private initiative, is fully free to set norms from a legal perspective, only bound to the opinion of its members. Yearly, WSW publishes its standards in advance (appendix VIII). Also, WSW works on the basis of facilitations volumes. This means that currently WSW determines an amount of financing (for a maximum period of three years) a corporation is free to attract. This replaces the financing on project basis since 2007. Hence, project norms are currently replaced by calculations based on revenues and pledges on the corporation level.

CFV is bounded by law to publish its policy rules in the Dutch government gazette. Amongst others, this has to include the methodology used for assessing a corporation's financial position (appendix VII). CFV describes its criteria in a fairly elaborate way. It only protects its norms. There are big differences between corporations, making no single set of norms appropriate for evaluation of the financial performance. Hence, CFV allows itself to vary its norms for individual corporations (appendix VIII).

Individual corporations have little influence in the norm setting. Norms are set based on expert judgment as well as past experiences. However, based on the end results combined with publically available information, corporations might gain insight in the norms used for the various information. They may use these norms themselves for monitoring their peers or they may approach CFV if they feel a corporation is weighted lightly. Still, this would require some serious focus and is most likely not the most efficient activity for peers.

#### *Detector*

In the collection of data (for standard regulation procedures), BZK, CFV, and WSW work together to limit the administrative burden for corporations. The three organizations base themselves, amongst others, on annual reports, auditor statements and specifically requested data of corporations. The specific data request, collection, preliminary quality analysis, and distribution is done by an organization called Corpodata. If corporations supply information wrongly, or with 'extreme' values, Corpodata checks with the corporation whether the information supplied is right. Apart from the identification of typos, this repeatedly also resulted in corporations adapting the data they provide. Corpodata has no formal legal status (appendix IX).

Through Corpodata, the ministry of BZK, WSW and CFV receive data twice a year. Before the first of February, corporations hand in prospective information in the dPi (Dutch: 'de prospectieve informatie' (Corpodata, n.d.b)). Before the first of July, information on the accountability is to be handed in, known as the dVi (Dutch: 'de verantwoordings informatie'. Both the dPi and dVi data are to be accompanied by board statements. In case of the dVi, also assurance reports, financial statements and an accountancy statement are required in addition (appendix VIII).

Not all information gathered by Corpodata is shared with all three requesting organizations. WSW asks its members for some specific data, as does CFV. The majority of information, however, is shared across all three organizations (appendix VIII). The data that is requested by BZK and CFV is specified in the appendices of the BBSH (accentuated in figure 5.3) (appendix VII). The distribution of gathered data is schematically represented in figure 5.3.

Furthermore, regulators have contact with corporations. From these contacts, corporations provide more detailed information of themselves but also have the ability to provide information of peers. The level of formalization differs per regulator. CFV visits corporations once a year, providing the ability to put this issue on the table. Furthermore, just as with WSW, corporations are free to approach the DA or account manager respectively (appendix IX).

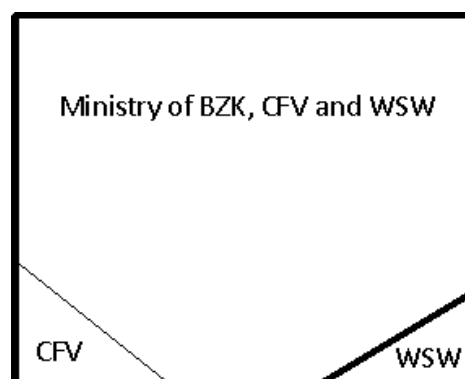


Figure 5.3: Schematic representation of the division of gathered data.

Basically, most information collected by regulators is non-confidential. Excluded are the accountant statements and detailed financial information. For the dPi request, corporations have the opportunity to label specific information as confidential for non-regulators (CFV, 2010a). CFV yearly publishes various reports on corporation performance. This includes reports on the sector performance in term of realization, but also the CiP reports for each corporation individually. In the CiP reports, a corporation is benchmarked against its geographic peers and activity like peers (e.g. specialized in care housing). These reports are publically accessible through the CFV website and thus available to peers (appendix VIII).

In conclusion, BZK, CFV and WSW work together in their basic request for data through Corpodata. Most of this information is non-confidential, making various analyses publically available to corporations. Hence, peers have the ability to collect extra information of one another. However, they don't have an information advantage in comparison to the formal sector regulators (in terms of financial position).

### *Effector*

Each of the regulators has multiple sanctions available. The disciplining means of BZK are mainly based on the corporation statutes that, by law, are to be agreed by the minister. Still, the means are fairly limited. BZK may appoint an external regulator in case of serious financial issues as well as add or remove persons in both the supervisory as executive board (appendix VII). In case of smaller individual infringements, BZK practically only asks for resolving the issue (appendix IX). By law, the minister is also capable of withdrawing the status of the corporation (appendix VII). In practice, however, this is hardly possible. In such case, it is unclear how to deal with the equity of a corporation, its employees and its loans. It is therefore that this option has never been used so far, and is unlikely to be used in the future. Hence, this option is not considered an actual enforcement measure in this research. In conclusion, BZK falls short in the more compliant measures.

The objective of CFV is to safeguard the continuity of the sector. However, CFV only has means to intervene in order to secure information, i.e. collecting data (appendix IX). Basic enforcement is done by regular monitoring and focusses on the continuity and solvability judgement. In case of concerns, CFV might require corporations to come with a recovery plan. Negative judgements may act as warning. In case of serious issues, the most extreme measure of CFV is intensified supervision. These issues do not necessarily have to be strictly financial, but may also concern governance or risk management. Besides being the financial supervisor, CFV also provides funds for financial restructuring. Though not a real penalizing measure, the financial restructuring of a corporation can be considered the most extreme intervention of CFV as it most definitely has a penalizing effect. By

financial restructuring, CFV will provide financial support to restructure the corporation and help it to become solvent again (appendix VIII). This often goes with the selling of a lot of equity to either peers or the market (Conijn & Kramer, 2010). By law, the funds of CFV are financed by the corporations themselves (appendix VIII). Hence, the financial restructuring can be considered as a peer monitoring arrangement (although it actually functions as a deterrent measure on peers instead of the corporation of subject). In conclusion, CFV appears to fall short in the lighter deterrent measures.

WSW is able to gently steer corporations in adjusting facilitation volumes (appendix VIII). Through this mechanism, WSW can practically withhold or stimulate a corporation to invest. When a facilitation volume is given, WSW still has the ability to temporize the investments of a corporations when it suspects investments may damage the financial position of the corporation and/or WSW. This is seen as a warning to a corporation. What is considered a penalty, is when WSW actually renounces (some of) the facilitation volumes. This gives a signal of WSW no longer having faith in the financial position of a corporation. Ultimately, when a corporation is in financial trouble, WSW may use the outstanding liability of other corporations to pay off the loans of the corporation in trouble (appendix VIII). In fact, this is a peer-to-peer mechanism that penalises the other corporations. When there are serious financial issues in a corporation, WSW might withdraw the creditworthiness statement of a corporation. This practically means that, in the opinion of WSW, the corporation is not solvent anymore. In fact, this is the prelude for a financial restructuring by CFV as the corporation will no longer be able to attract financial funding (appendix VIII).

In figure 5.4, an overview is given of enforcement measures that can be taken by the various corporations. What strikes the eye, is that over the entire sector there appears to be few available 'penalties'. Where more persuasive measures have a relatively low obligation to comply and seem to focus more on the financial position, the more stringent measures seriously infringe the legitimacy of a corporation and do address governance issues more. Furthermore, there are few formal and effective peer-to-peer arrangements. Of the three arrangements identified, actually the AEDES codes and the withdrawal of the AEDES membership are the only arrangements through which peers can formally influence a corporation. The financial restructuring support of CFV is an arrangement that makes peers financially accountable for a corporation, thereby theoretically stimulating them to use other arrangements to make a corporation comply. Hence, from this analysis it is concluded that though peers are accountable, they themselves have no formal means for intervention. However, indirectly, peers may stimulate other regulators in applying other sections existing.

In conclusion, the enforcement measures that may be imposed on corporations are spread over different regulators. The system seems to fall short in the penalizing measures on financial performance. Peers have no formal place in the application of sanctions by regulators. Their means are outranked by a far bigger variety of more practical measures that can be taken. Still, they may stimulate regulators in applying sanctions and therefore contribute to informal regulation.



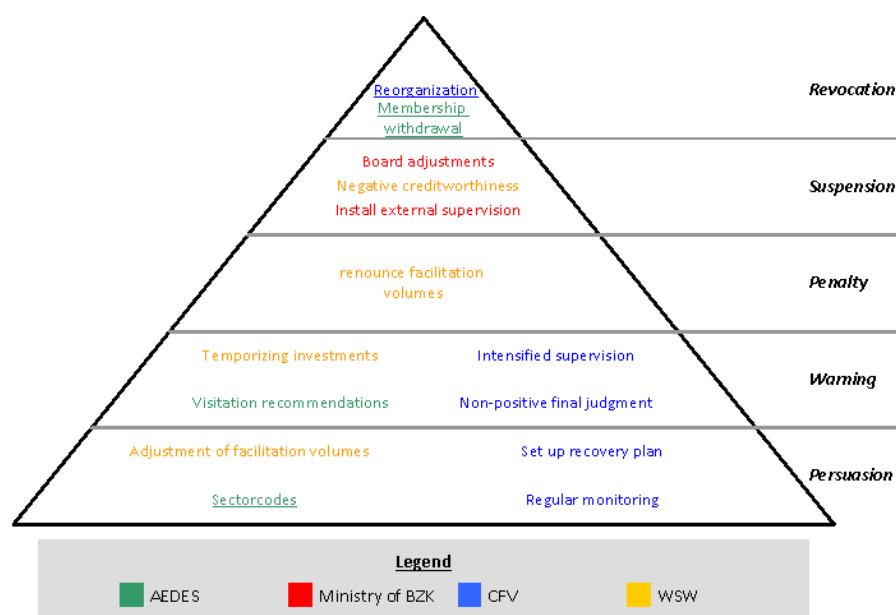


Figure 5.4: Schematic categorization of enforcement measures (underlined are considered peer-to-peer arrangements)

### 5.3.3 Notions for the propositions

Peer monitoring is to take place in a context in where three other, more formal, regulators exist. Two of these regulators also put significant effort in corporation risk taking. The existence of (multiple) ‘vertical’ regulators reduces for willingness for peer to ‘horizontally’ regulate one another. Especially when it comes to moral hazard as two of the regulators focus on corporation risk taking specifically.

In the ability to establish ‘directors’, peers are not really dependent on regulators or vice versa. Although corporations are free to gain insight in the way of working of regulators. This way, they are potentially able to identify loopholes and regulate each other on them. However, the information position of regulators turns out to be very relevant. Due to competitiveness, corporations shield a lot of information (particular on risk taking) from each other. Much of the information regulators use is made public, just as the analysis done based on this information. Considering the limitations in peer monitoring, this significantly widens the opportunities of peers to be informed of one another. Considering sanctioning, regulators also prove to have a far wider and more practical arsenal available than peers. Peers are currently of no formal use in applying sanctions. However, informally there is the possibility for peers to let a regulator engage in an intervention.

## 5.4 Institutional context of peer monitoring in the sector

In the functioning of regulation, Baldwin and Black convincingly argue the context to be of significance (section 3). As start for the functioning of peer monitoring as regulatory arrangement, the previous section already elaborated on the most obvious element of the context: other regulators in place. This section further elaborates on the embedding of peer monitoring in the remainder context.

In relating Baldwin & Black to the Williamson model on institutions, it was shown that regulatory arrangements find their place in between the institutional environment and day to day practice (section 3). This section first discusses the implications of the institutional environment on the functioning of peer monitoring. Second, it discusses the day to day complexity in the regard of peer monitoring. The section ends by relating the section findings back to the propositions.

#### 5.4.1 The institutional environment and cultural embeddedness in the sector

The work of corporations is embedded in the Dutch law on housing that was introduced in 1901. The original objective of corporations is to improve living conditions by stimulating the build of new and proper houses for the weaker of society. Social housing started as a private activity by the rich to facilitate their workers, but grew into a governmental activity quickly. In 1983 the right on housing was embedded in the Dutch constitution as a public responsibility (appendix VII). Social housing has long been a task dedicated to municipalities (appendix VI).

Since the financial autonomization, corporations are social enterprises operating more in a market environment. This created a bandwidth of corporation cultures between those still closely connected to the municipality and those making full use of the market opportunities (appendix VI). The opportunities and limitations for corporations are described in the current version of the law on housing. The law had its last major reform in 1991. It is effectuated by two governmental decrees: BBSH and BCFV (appendix VII). The latter discusses the functioning and responsibilities of CFV, the regulator already discussed in 5.3. Therefore, here only BBSH is elaborated on further.

BBSH describes the activities a corporation may engage in. Important in respect to DAEB regulation is that there always is a link between government means (which includes the WSW guaranteed loans) and the projects invested in. This provides ground for peers to monitor each other on. Corporations may engage in a variety of activities, the following list just names three examples (appendix VII):

- Building, acquisition, and demolition of housing and appurtenances
- Maintaining and provisioning of housing and appurtenances
- Maintaining and improving the direct adjacent area of housing and appurtenances

In its essence, social housing is a non-profitable business. However, after the autonomization, corporations were seen as very rich entities. Hugo Priemus observes this in practice: ‘While many town halls deteriorated, the architectural quality of corporation headquarters improved’ (Priemus, 2013). This was also a direct consequence of BZK policy (under the heading of Johan Remkes) (appendix VI). Through Remkes, corporations were bound to building half of the demolishment while selling more, in a time of rising real estate values (Boelhouwer, 2013).

The non-profitable core of corporations made them willing to compensate by engaging in more commercial activities. Over time, politics allowed this engagement by a number of adaptations to the BBSH. Basically nearly all real estate projects can apply for corporations to engage in. In its current form, corporations gained a number of freedoms in addition to the previous list. Below, just some opportunities are listed (appendix VII). Notice the link with the listing above:

- Building, acquisition, and demolition of non-housing buildings
- Maintaining and provisioning of facilities on non-housing buildings
- Maintaining and improving the environment outside the immediate vicinity of housing

These freedoms gave corporations great leverage in commercial activities. It made the sector culture transpose in one tempted by ‘glitter and glamour’ (Elsinga, 2013). In these commercial activities, corporations also had a head start as they can benefit from cheap financing and miss real focus on their returns. Currently European regulation again limits these opportunities somewhat by their regulation on these activities and the state guaranteed financial means of corporations (appendix VII).

### 5.4.2 The multi-actor network in the sector

In chapter 3, it was already argued that regulation is only part of motivation for behaviour of an actor. This paragraph elaborates on stakeholders not discussed earlier in this chapter that are potentially very relevant in managing moral hazard through peer monitoring in the Dutch corporation sector. The text in this paragraph is mainly based on findings of the actor analysis performed in appendix IX.

#### *Accountant*

The accountant is responsible for the quality and correctness of the corporation's financial statements. In this research, the term accountant is used for the external accountant. The internal accountant is referred to as auditor. The accountant is the external organization best informed on the financial situation of a specific corporation. Hence, the accountant statements are important for the current formal regulators.

However, the accountant is in a dilemma. Its job is determined by law and there are specific standards to follow determined by the accountancy council. On the other hand, the accountant is directly paid for by the corporation itself and is experiencing competition from other accountants. Over the years some doubt arose on the well-functioning of accountants in evaluating financial statements of corporations. It was suggested that some ignored risk and delivered low quality (of even fraudulent) reports. It indicates some accountants may be sensitive for their client desires. It directly lowers quality at formal regulators, thereby increasing the risk of moral hazard when the accountant is a 'false' safety net.

#### *Corporations*

So far, little attention was given to the complexity of peers monitoring each other. From the concept of peer monitoring, it is already clear there is not just a single corporation in the Netherlands. The number of peers appears relevant in the functioning of peer monitoring. In 2002, the Netherlands counted 552 housing corporations (CFV, 2003). Because of mergers, the number of corporations dropped to 389 in 2012. Together, these 389 corporations operate a near 2,5 million housing units, almost a third of the total Dutch supply (CFV, 2012b). The 50 biggest corporations own about half of the total amount of housing units owned by corporations. Many corporations specialize themselves in a certain activity, e.g. care housing, student housing or neighbourhood restructurings (appendix IX). Furthermore, most operate in geographically distinct areas (appendix VII).

The amount of corporations in combination with the level of detail needed to monitor the risk taking behaviour of a peer makes it very costly for a corporation to monitor its peers. In fact, it seems practically impossible. The geographical distinction in operation adds to this. A second effect is risk dispersion. When risks are dispersed over such a large group, the consequences for peers stay relatively limited. Third, the specialization of corporations raises questions to the comparability of corporations.

Furthermore, corporations are interdependent on more ways than through the financial security structures only. Corporations engage together in projects and have opportunities to cross-finance the projects of one another (appendix VIII). Also corporations active in the same municipality often have strong ties to that municipality. The corporations work together in fulfilling the social housing assignment of the corporation (appendix IX). Often corporations are also often politically active (Calon, 2012). These interdependencies obviously have implications for the functioning of peer

monitoring. They might ease the information gathering of corporation on peers. Hence, it may contribute to the detector element in peer monitoring. On the other hand, it may complicate and reduce the willingness for intervention. Hence, it may reduce the effector potential of peer monitoring.

All corporation executive boards have some form of internal regulation, which is mostly taken care of by the supervisory board. The supervisory board has four type of responsibilities to the executive board: employer, advisor, controller and networker. Obviously, it is hard for a supervisory board to proper balance itself between its advisor and controller activities. However, supervisory board members of most corporations are gathered in VTW. This provides opportunities for peer monitoring.

#### *VTW*

VTW is founded in 2002 as a professional body for those responsible for the internal governance of housing corporations. VTW has around 1600 members that are member of the supervisory boards of over 320 housing corporations. VTW sees itself as a centre of expertise and knowledge and has the objective to contribute to a strong, independent and professional internal governance of housing corporations. For this reason it organizes discussions, workshops etcetera, and cooperates with organizations as Aedes, CFV and BZK (appendix IX). NVBW is the comparable (though less active) organization for members of the supervisory board of corporations (NVBW, n.d.).

VTW is an opportunity for the functioning of peer monitoring. It was shown that it may be hard for peers to regulate each other because of various interdependencies. Generally, supervisory board members are slightly more removed from the day-to-day corporation practice. Also, it is one of their core activities to regulate on their own executive boards. This potentially reduces the sensitivities in the exchange of information and allows for more subtle informal interventions. However, no such activity is explicitly found in the current system.

#### *Municipality*

Municipalities formally act as the contracting authorities for corporations. As such, they also play a role in the supervision of corporations. However, this role is fairly complex because of two reasons. First, already argued, corporations engage in more non-DAEB activities. This gives negotiations more of a double role. Traditionally, municipalities assign land to a corporation to develop social housing. Currently, negotiations are held on the amounts of lands for social housing in trade for land on commercial activities for different prices. Second, municipalities experience financial stress, making them willing to do profitable business with corporations. As a consequence, municipalities to some extent incentivize corporation risk taking behaviour.

As said, traditionally the municipality assigns land to a corporation for developing social housing. Since the financial autonomization this is shaped through municipal performance contracts. A municipality is to have a contract with each corporation in its region on its social performance over a specified period. Combined, these contracts comply with the strategic housing policy of the municipality. In practice, this is no unilateral relation. For previous named reasons, corporations often co-develop this policy with the municipality. Although this reduces the potential role of the municipality as regulator, it also offers chances for peer monitoring to function. From the performance contract, the municipalities have opportunities to intervene. The corporation involvement enables them to have more information on their peer performances and contributions. As such, peers are in a better position to informally approach the municipality to intervene if they deem this necessary.

### **5.4.3 Notions for the propositions**

Since the financial autonomization, the corporation culture is in transition towards a more competitive one with risk taking as logical and accepted consequence. Through lobby, corporations are now also allowed to engage in a variety of commercial activities. This makes it less clear on what is not allowed for corporations to engage in, making it harder for peers to monitor while giving corporations more opportunities to take risk.

Also the monitoring of peers proves to be complex and costly, if at all possible. Currently, The Netherlands counts 389 corporations specialized in different activities and operating in different regions. Vice versa, the amount of corporations risks are spread over also lowers the incentive to regulate one another. It also proves corporations are interdependent on more than the financial security structures only. Though this increases the information position of peers, it hampers the willingness of peers to intervene at one another.

Corporations also prove to be strongly interdependent with the municipality and with each other through the municipality by the co-development of strategic housing policies. This reduces the potential of peers to discipline one another, but it increases the potential of peers gathering information of one another. It enables peers to be better informed on one another. It also gives them access in an informal way to an extra arsenal of potential enforcement measures.

## 5.5 Proposition results based on the institutional analysis

In table 5.1, the preliminary notions identified in this chapter are summarized per section. This section summarizes these findings of the institutional analysis based on the propositions studied in this research. As such, each proposition is discussed separately in the paragraphs of this section.

Table 5.1: Summary of notions for the propositions based on the institutional analysis

Section	Preliminary notions
Moral hazard in the Dutch social housing sector	<ul style="list-style-type: none"><li>- Competitive sector setting</li><li>- Easy access to cheap financing</li><li>- Sharing of negative consequences</li></ul>
Peer monitoring	<ul style="list-style-type: none"><li>- Accountable for one other's losses</li><li>- Few direct means to discipline peers</li><li>- No voluntary sharing of information</li></ul>
Regulatory context of peer monitoring in the sector	<ul style="list-style-type: none"><li>- Vertical disqualifies horizontal</li><li>- Vertical regulators publish data</li><li>- Regulators operate redundant</li><li>- More means to intervene</li></ul>
Institutional context of peer monitoring in the sector	<ul style="list-style-type: none"><li>- Legislation allows many freedoms on risk</li><li>- Risk is dispersed over many peers</li><li>- Mostly only regional peer contacts</li><li>- Multiple interdependencies exist</li></ul>

### 5.5.1 Peers have sense of urgency to regulate one another

The accountability of peers through the financial security functions provides a strong incentive for peers to regulate one another. Other financial interdependencies, for example through the co-participation in projects and collegial financing can strengthen this incentive.

However, these incentives can also work vice versa. In the risk of supporting peers, peers may not regulate one another in the hope risks 'turn out right'. This feeling is strengthened by the existence of a number of different regulators. Two regulators, CFV and WSW, focus on the financial performance of corporations specifically and the municipality is also monitoring the performance of the local corporations. The sense of urgency of peers to regulate another is further reduced by the big amount of corporations in the Netherlands, as 1) the big amount of corporations makes monitoring complex and costly and 2) it makes that risks are spread over many corporations, directly lowering the incentive to regulate one another.

Also, the variety of activities in which corporations are engaged in, makes it harder for peers to determine on what is acceptable and what isn't. It requires norms more on the level of quantity of activities than type of activities. As corporations are diversified, peers are less willing to set standardized norms.

### 5.5.2 Peers have information about each other's behavior

The corporation world proves to be a small one. Peers are gathered by national meetings of branch organization Aedes. Most of them are also gathered in regional gatherings, especially in the more municipal areas. This makes that the executive board members of corporations know each other and are fairly aware of the ambitions and activities of their peer corporations. Since the autonomization, corporations are more competitive to each other, making detailed information, especially financial

information, strategically valuable. However, CFV yearly publishes a number of reports. These also concern individual information and the underlying information can be made publically available.

All in all, it appears corporations might therefore have quite some information on the performance of peers. However, it is still so that peers are not in a better information position to regulate one another compared to formal regulators. Especially in terms of level of detail of information on the financial performance, peers prove to lay behind compared to CFV and WSW.

#### **5.5.3 Peers may interfere with each other's business**

From the security functions and other interdependencies between corporations, it is expected that peers are to some extent willing to interfere at each other. However, there are also incentives that lower this willingness, mainly driven by the existence of formal regulators. In addition, also the idea that corporations have to work with each other for longer times (as competitive colleagues) and are interdependent on other aspects than financial support add to this.

#### **5.5.4 Peers have formal and informal means to intervene**

Formally, there are few things peers can do to intervene at one another. Effectively they have influence on the sector codes provided by Aedes. However, in case of non-compliance to the code, the only penalizing measure of Aedes is to withdraw a corporation's membership. Furthermore, peers may formally influence the norms set by SVWN for corporation visitations. Also peers may approach each other directly. However, with no formalized sanctioning mechanisms in place, the effectiveness of these activities is doubted.

Informally, peers may utilize a variety of sanctions available to the regulators. The combined regulator sanctions vary in their focus on compliance and deterrence. Still, the ability to apply the softer penalizing measures is limited. It is questionable how well peers may utilize these means, as they are not formally involved in the regulation process. In conclusion, the means available to peers to intervene at one another are fairly limited.

#### **5.5.5 Peers have enough degrees of freedom to adjust regulation to the situation at hand**

Peers themselves have fairly limited options available to discipline their peers. Formal regulators have options available, but peers are not formally incorporated in the formal regulator regulation process. Hence, peers are dependent on their informal strength. In this informal influence peers may have, undoubtedly a lot of nuances get lost. In fact, it is at all questionable if peers have the information available to discipline each other according to the situation at hand. Hence, it appears that the responsiveness, i.e. the degrees of freedom of peers to adjust regulation to the situation at hand is fairly limited.



## 6. Case study

From the institutional analysis, it already proved the answers to the propositions are not as straightforward literature suggests. This chapter studies the functioning of peer monitoring in influencing risk taking decisions, i.e. managing moral hazard, for the practice of three Dutch corporations: Servatius, Eigen Haard and WSG. The propositions are discussed for each corporation in the subsequent sections. Each corporation is briefly introduced. The propositions identified in chapter three form the basis for the paragraphs of the section. The chapter concludes with a comparison on the different corporations studied.

### 6.1 Woningstichting 'Servatius'

Servatius is the second largest corporation (operating almost 12.000 vhe) operating in the south of the Limburg province. The corporations actively engages in projects and group positions. In 2008, the corporation came in solvability problems due to a downturn in over 80 highly complex and non-transparent projects. A more detailed description of Servatius is found in appendix X. This section further elaborates on the peer monitoring propositions specified to the Servatius case.

#### **Proposition 1: Peers have a sense of urgency to regulate one another**

##### *Lack of precedent*

The security functions in the sector have been existing for years. Also before the autonomization, corporations were supported (and backed) by state aid through subsidies etc. Servatius knows that in extreme cases it might have to pay for other corporations just as Servatius knows other corporations might have to pay for Servatius. Apart from knowing, it is questionable whether Servatius was really aware of this arrangement and its potential impact (confidential source). "The security structure has been ever existing but not used much. Maybe, it would be good if a corporation would go bankrupt once. However, this is currently not possible" (confidential citation). Even when corporations had to pay for the financial security structures, these payments were small compared to the benefits of the structure (confidential source).

##### *Reputation issues*

Leks Verzijlbergh (i.e. the executive at the time) was a celebrated and respected man in the Maastricht community who already proved his capabilities (confidential source). He was a man dedicated to social housing, a man with vision and ambitions (confidential source). The campus project was supposed to be one of his crown-jewels (confidential source). A misstep would lower the status of Verzijlbergh (and, hence, improve the relative position of peers). The campus project would "most definitely bring him status. At least, if he had succeeded" (confidential source).

Servatius did not significantly comment on risk others took, nor did it significantly receive comment beforehand or during projects (confidential source). At least not on the two best known project bringing financial problems to Servatius: the campus project and the Lambertus church. It is only when it became clear the project turned out bad, peers started to raise critique on engaging in the project in the first place thereby claiming they 'knew' it would go wrong (confidential source). Hence, no real sense of urgency seems existing.

##### *Vertical disqualifies horizontal*

To some extent, the reputation issues between the Maastricht corporations makes them allow each other to take on risk (confidential source). And the formal freedom of corporations to engage in risk is large (confidential source). It is considered to be the responsibility of the regulator to prevent any

missteps so severe it would have consequences for others (confidential source). Hence, formal ‘vertical’ regulators set a context that limits the sense of urgency of peers to regulate each other (in a ‘horizontal’ way).

#### *Proposition conclusion*

It appears there was no real sense of urgency for peers to regulate Servatius. Over time, there have not been any financial restructuring cases in Limburg and barely any in the Netherlands. Furthermore, the Servatius managing director was a well-respected man in the regional network. A misstep in one of his projects, especially a crown-jewel, is an effective way to level his status to the others. Serious financial issues are considered to be prevented by the responsible formal regulator.

### **Proposition 2: Peers have information about each other’s behavior**

#### *Only information of regional peers is gathered*

The Maastricht corporations come together in informal regional meetings (confidential source). In these meetings, they discuss the issues and developments in the region (confidential source). Another example of the regional meetings is Parkstad (confidential source), a meeting of corporation active in the former Dutch mining areas (Parkstad Limburg, n.d.). From this meetings, corporations gain some outside knowledge on activities of the other (confidential source). However, the informal meetings are very policy related. Though, since roughly two years, more information on each other’s performance is shared (confidential source). Participation in the group as well as sharing information and issues is on a voluntary basis (confidential source).

#### *No voluntary sharing of information*

“If another corporation engages in a larger project in the same region, a corporation knows. However, corporations only have outside knowledge and no clue on practical arrangements and financial performance” (confidential citation). Information is not shared voluntarily as it is strategically valuable (confidential source). Peers are not in position to study each other’s books, making them dependent on the willingness of an individual corporation to share its own performance (confidential source). Up until some years this was just not done. Since some years, issues are discussed more openly and transparent (confidential source).

#### *Information spread over organizations*

Another way peers gain information on Servatius (and vice versa) is through the municipality and project developers that approach corporation with their ideas (confidential source). “In developing larger projects, other corporations mostly know because these projects are co-developed with the municipality or project developers” (confidential citation). In this sense, other corporations were also aware of the campus project (Verzijlbergh, 2011). However, Maastricht corporations appear to have no inside information on the progress and results of activities (confidential sources). Corporations have practically no insight in the operations of non-region corporations. Servatius only operates in Maastricht. Hence, they are purely focused on Maastricht developments. They are barely interested in other regions as they have a formally clearly demarcated operating area (confidential source).

Information is spread over the actors. Woonpunt and Servatius have more knowledge than non-corporations on each other’s individual projects and regional developments (PCO Advies, 2010). However, on the overall corporation performance, regulators as CFV have the most information (confidential source). Regulators, together with accountants, are the only ones that have access to

the actual financial administration (confidential source). In fact, it appears Maastricht corporations know less of each other than what is publically available (confidential source).

This mainly comes down to the interest of the organization. A regulator is generally not interested in a specific project, unless the financial performance gives reasons to do so. Peers have no feeling of monitoring each other (see the other propositions) but want to mirror themselves to comparable other corporations. This is mainly a status issue. Status is not gained by financial performance, but by 'crown-jewel' activities. The campus project is a good example of such a project (confidential source).

#### *Proposition conclusion*

Peers have general information on the activities of Servatius that they gain through interaction with each other, the municipality or project developers. Peers have few information on the general Servatius financial performance because of a lack of interest and Servatius protecting its information. Outside this region, there is even less transparency on corporation activities (confidential source).

### **Proposition 3: Peers may interfere with each other's business**

#### *Autonomy*

Servatius, and the other peers in the Maastricht region, tolerate no form of regulation on one another whatsoever. Formally, interference is not formally arranged, it is absolutely not-done (confidential source). But also informally, critique to and from Servatius is not tolerated in the regional setting. Recently, the managing directors of two corporations approach the managing director of a third corporation to question him on a new activity he engaged in during a dinner. Until some years ago, this would not have happened. However, the dinner was not much appreciated (confidential source). "One may expect corporations to discipline each other as they strive the same objective. However, they are autonomous organizations with their own strategies and objectives just like every other organization" (confidential citation).

#### *Reputation issues*

Status is an important issue for the Maastricht corporations and their managing directors. Ultimately this status is built by big fancy projects. "A project of 200 social housing units is just incomparable to the status a successful campus project would have brought" (confidential source). This makes that risk taking is allowed in the network, also on project that not directly contribute to the corporation's core. Hence, Maastricht corporation are together in building status and therefore in no position to criticize one another on risks taking (confidential source).

Also based on status, Maastricht corporations (to some extent) like Servatius bleeding (and vice versa). A bleeding Servatius raises the respective status of other corporations to each other, but also to external organizations like the municipality. The limit is reached when corporations experience negative consequences themselves. Note this not necessarily means Maastricht corporations having to pay for each other (confidential source). Significant cuts in the social capital of Servatius also hampers the peers in their functioning (confidential source). "Corporation now complain as Servatius is selling much houses, thereby disturbing the market conditions" (confidential source). So, also the selling of vhe (of Servatius) to finance the losses of Servatius on the campus project hampers peers as it disturbs the regional market (PCO Advies, 2010). Unlike profit organizations, corporations are unhappy when the activities of others are under pressure (confidential source). In other words, the corporations surrounding Servatius are hampered in their financing as Servatius is selling equity at discount to finance its losses on the campus project.

#### *Proposition conclusion*

Servatius and Maastricht corporations in general, accept no form of peer interference. The main explanation seems to lay in status. Building and protecting relative status of the individual Maastricht corporations, risk taking is allowed (or even a necessity. Also, bleeding of a corporation is considered favorable as long as it does not hamper the activities of peer corporations.

#### **Proposition 4: Peers have formal and informal means to intervene**

##### *Lack of effective direct means*

“Even if a corporation wants to discipline its neighbor, there is no formal ground to do so” (confidential citation). The previous proposition already showed the limited capabilities of a direct informal approach. Indirect, there seem to be two opportunities of Maastricht corporations to intervene in Servatius (or vice versa) in an indirect way (confidential sources).

##### *Third parties provide means to discipline peers*

First, corporations may approach the municipality. The Maastricht municipality performance contracts with the Maastricht corporations (confidential source). This contracts are often bundled to a (publically accessible) plan of the municipality in which the contribution of the respective corporation is specified (confidential source). In the case of Servatius, there is a single contract between the corporation that specifies the city needs and the individual contribution of a corporation. When Servatius not realizes promises, this might be an indicator of problems. Peers can then approach the municipality in an informal way to intervene (PCO Advies, 2010). The second option is to share the opinion with CFV. In practice, this is always done in the light of a regular visit of CFV to a Maastricht corporation where that corporation starts talking of other corporations, e.g. Servatius, in the margin of the conversation as “the relation has to be built with care”(confidential source).

##### *Peers approach regulators only informally*

“They won’t call or mail, but it might surface ‘by accident’ in a regular visit. It is no standard issue discussed, that might be a good idea” (confidential source). Often lacking substantiation (“signals are mainly just frustrations that are communicated”), it is the call of the individual CFV regulator to use or not use this signal (confidential source). The implication of this limit is shown by the campus project of Servatius. The campus project had to be (and was) approved by the ministry (who was advised by CFV) (PCO Advies, 2010). Starting the project, the project turned out to be bigger, calculations were incorrect and the managing directed withheld this information (confidential source). “When decisions were made I heard nothing. It was only when things turned out wrong other corporations started complaining” (confidential citation). Typically, CFV visits corporations once a year. The campus project turned bad within a year and some corporations explained they saw this coming (confidential source). CFV did not receive signals of corporation up until their next visit. Peers did not engage to CFV to share their suspicions (confidential source).

#### *Proposition conclusion*

Maastricht corporations have a very limited arsenal to intervene at Servatius. Lacking formal means and direct informal means not being tolerated, basically two informal indirect means remain. Peers may approach the municipality when a corporation, e.g. Servatius, is not living up to the performance contract and they suspect this being evidence of larger problems. Second, they might approach CFV. However, also then Maastricht corporations are limited by the inter corporation culture limiting the effectiveness of these means.

### **Proposition 5: Peers have enough degrees of freedom to adjust regulation to the situation at hand**

Maastricht corporations have a limited arsenal of means to intervene (confidential source). The culture and drive for status limit the usability of these means even further. Therefore, even though some degrees of freedom are present, barriers to utilize seem to be so high that peer regulation cannot be considered responsive (confidential source).

## **6.2 Woningstichting 'Eigen Haard'**

Eigen Haard is one of the larger corporations in the Netherlands (operating over 56.000 vhe) and operates in the Amsterdam region. The corporations actively engages in projects and group positions. Still, it is performing better than many of the other corporations. A more detailed description of Eigen Haard is found in appendix XI. This section further elaborates on the peer monitoring propositions specified to the Eigen Haard case.

### **Proposition 1: Peers have a sense of urgency to regulate one another**

#### *Lack of precedent*

Eigen Haard knows that through the sector financial security structure, it might have to pay for other Dutch corporations. Since Vestia, Eigen Haard is painfully aware of this arrangement. For Vestia, Eigen Haard to contribute around €16 million (confidential source). It is questionable whether Eigen Haard was really aware before this time (confidential source). "We have experienced a period longer than 10 years in which barely any financial restructuring support was needed. Economic conditions made corporations somewhat lazy"(confidential citation).

Over the last ten years, there has barely been made any claim on the financial restructuring fund of CFV. Till some years ago, SGBB was practically the only corporation peers had to pay for (confidential source). Still, the contribution to SGBB was fairly limited. As there have not been many claims, there has neither been a significant contribution to CFV (confidential source).

On top, Eigen Haard, amongst with other Dutch corporations, had benefitted from the good economic conditions and rising real estate value. This made corporations less attentive. The Vestia case represents the moment of change (confidential source). However, the Vestia case made corporations look to their internal governance more than monitoring on peers (confidential source).

#### *Vertical disqualifies horizontal*

Monitoring of corporations is the core activity of regulators as CFV. "A case like Vestia makes corporations oppose to our functioning. Still, they don't look to each other" (confidential source). In Amsterdam, corporations gossip on others. However, formally they make no statements (also not after Vestia). Though hard to prove, it is almost unimaginable Eigen Haard did not know of integrity issues at some other Amsterdam corporations (confidential source). Since the Vestia case, corporations have more sense of urgency to regulate one another. In fact, this topic has been explicitly discussed in a gathering called De Vernieuwde Stad (confidential source). De Vernieuwde Stad is a gathering of 23 large Dutch urban corporations that includes the six largest Amsterdam corporations (De Vernieuwde Stad, n.d.).

#### *Risk dispersion over many peers*

"We shouldn't forget the Netherlands counts more corporations than the six in Amsterdam. Eigen Haard may be hit just as hard by any corporation in the Netherlands. It proves already hard to be

informed on your direct peers, nationwide it is just impossible” (confidential citation). Still, risk is shared over the whole Netherlands. This reduces the sense of urgency further for two reasons. First, the risk of direct peers is shared over the entire country (confidential source). Second, other peers are better in monitoring corporations in other parts of the country (though these also experience both these elements) (confidential source).

#### *Proposition conclusion*

Eigen Haard knows it might have to pay for others. However, it appears the awareness of this obligations blurred over time in lack of claims and favorable conditions for corporations. After Vestia, the awareness on the financial link between corporations revived. Still, there is no real sense of urgency to regulate one another as formal regulators exist and risk is spread over many corporations.

### **Proposition 2: Peers have information about each other’s behavior**

#### *Reputation issues*

Eigen Haard is, like basically every other corporation, strongly focused on its own activities. This not only considers the monitoring of others, but also the learning of others. In general, corporations are busy more to differentiate themselves from others, i.e. pay focus to their unique difference (in the positive sense) in comparison to others (confidential source). “All Amsterdam corporations claim they are the best. In fact, according to their own metrics, they are” (confidential source). This is explained by the competition between corporations and complexity in financial performance. “Nobody scores well on every aspect as the context is very relevant. Thus, corporations do cherry picking” (confidential source).

Since Vestia and the crisis, this is changing. Corporations realize they can work together more (confidential source). Amongst others, this results in the Amsterdam corporations benchmarking their data, even the prospective data that is generally considered strategically valuable. Still, this sharing of information is shared on trust and, hence, sometimes anomalies are discovered (confidential source). However, it is a clear trend in the relations between Amsterdam corporations.

#### *Information is spread over organizations*

As a consequence of the strong internal focus, Eigen Haard as well as the other corporations have a broad sense of other corporations. However, it appears the Amsterdam corporations barely had a substantiated idea of the financial positions of others. Eigen Haard might have some ideas on the activities of others, but has no significant knowledge on the financial performance and risk management of others. “Much information is publically accessible, but corporations don’t invest in the information of peers. Managing a corporation is a full time business” (confidential citation). Through AFWC, corporations are quite aware of the activities of others. This also shows the relevance of the region corporations operate in (confidential source). More and more since 2010, financial performance and risk taking is discussed in the regional gatherings as well (confidential source).

#### *Internal focus*

Nor Eigen Haard nor any of the other (Amsterdam) corporations appears to use publically accessible information. The yearly statement of a corporation, CFV CiP analysis, CFV region analysis and BZK judgment are publically accessible. However, never in the Amsterdam arena, corporations were seen taking good notice of the position of others leading to a substantiated argument on others. Even in

the case of potential mergers, it is often new to the corporations when CFV supplies this information. However, this is changing since the Vestia case but is to be developed further (confidential source).

Information on the financial performance of the corporation in respect to its reference groups (including its geographical region) is often passed on to lower non-executive management (confidential source). Communication back to the executive or supervisory board is (at best) very rare. If it happens, analysis are often contested. “This is possible because of complexities, analysis only make sense when studied in coherence” (confidential citation). On top, focus again lies again on the internal function (i.e. proving the corporation is the best of others) in contrast to peer monitoring (confidential source). The strong internal focus combined with the cherry picking to be the best corporation also makes differentiation of the Amsterdam corporations look bigger than it actually is.

#### *Only knowledge of ‘similar’ corporations*

Still, the differentiation leads to ad hoc networks of corporations with similar interests. A good example is corporations actively working with derivatives (including Vestia and Portaal) (confidential source). Eigen Haard choose not to participate and keep a moderate derivative profile, as Eigen Haard felt active treasuring as not in line with its norms and values (confidential source). Still, having an active treasury policy is allowed (Rijksoverheid, 2012). Leaving Eigen Haard, it appears that also in these ad hoc networks, not much information is shared. “Never, corporations speak frankly” (confidential citation) Corporation executives often have a permanent contract and are sensitive for status. Hence, executives aim to hide their weaknesses to prevent them being ‘eaten by the market’ (confidential source).

#### *Proposition conclusion*

Eigen Haard had no substantiated information on the risk taking behavior of others. Regionally, the information of peers is best, but is still lacking behind on publically accessible information. This is explained by the strong internal focus of the Amsterdam corporations. Operating under competition, Eigen Haard, together with the other Amsterdam corporations, aims to differentiate themselves from the others. Hence, they do cherry picking on the information available to prove they’re the best and disguise their weaknesses. Peer monitoring is of no focus in information gathering and giving knowledge to that information. Since 2010, this is changing.

### **Proposition 3: Peers may interfere with each other’s business**

#### *Autonomy*

Eigen Haard feels itself not in the position to (formally) judge on the position of other corporations (confidential source). From the idea that everybody has its own responsibilities, it is not done to interfere in the (execution of) responsibilities of the other. “A corporations managing director may be vain or not, one of his core activities is to protect his status in the group” (confidential citation). This should also be the added value of a regulator (confidential source). In case of Eigen Haard being involved in a project of another corporation (i.e. has a participation share) this statement might be slightly nuanced. However, non-intervention remains the leading principle here as well, unless interference might lead to a positive sum-game. A zero sum-game is not considered sufficient (confidential source).

Apart from Eigen Haard, and the Amsterdam corporations in general, a typical example of corporations in Friesland is provided. To gain insight, a regional group of Friesland corporations set up a benchmark of the Friesland corporations. This discussion on who performs best led to such



disputes between the corporations, multiple left the regional group. Note the objective of the benchmark was to gain insight. It did not serve for any peer interference on corporation policy whatsoever (confidential source). However, in AFWC and De Vernieuwde Stad, the opportunities of corporations to discipline one another are more discussed since the Vestia case (confidential source).

#### *Vertical disqualifies horizontal*

Because of the existence of a regulator, a corporation agitates on policy instead of other corporations (confidential source). On top, risk is shared nationally. It is impossible for Eigen Haard to get a nationwide overview. Also this is why a regulator is existing (confidential source). Together with WSW, CFV is to set boundaries and do signaling. “It is the job of the supervisor to monitor. Corporations have the right to depend on this. Hence, they are also in the position to be mad at supervisors” (confidential citation).

#### *Interference requires deep knowledge*

Furthermore, interfering in each other’s business is also hard as it requires deep knowledge on the management of that respective corporation. The previous proposition already showed Eigen Haard does not have this knowledge. Hence, the opinion of Amsterdam corporations on others is often missing the nuances. “They all gossip in the absence of the other, it is rare this exceeds the level of bar talk” (confidential citation). Even more basic than peer monitoring, corporations in general should start to learn from each other more (confidential source). Many invented wheels themselves, while so much information is relatively easily accessible (confidential source).

#### *Reputation issues*

In general, corporations are competitive to each other. Since the downturn in the real estate market, this is somewhat changing (confidential source). Eigen Haard does not regret that many of the other Amsterdam corporations are under intensified supervision. It distinguishes them from their peers (competitors) in a positive way providing them extra opportunities (as the municipality of Amsterdam will try to keep its activity pattern intact). “In the Amsterdam region, Eigen Haard is gaining significant status because of the problems of others. This should not be underestimated” (confidential citation). The Amsterdam corporations compete on social relevance and stature. It is often the smaller corporations, like Driemond, who operate more from an idealistic approach. Note this observation might change when Eigen Haard has to pay for the other corporations (confidential source). “Eigen Haard will ‘like’ the bleeding of other corporations as long as they don’t need to be infused” (confidential citation).

#### *Proposition conclusion*

Four reasons are distinguished that hamper Eigen Haard from interfering with their peers. First, it is simply not done. Only very exceptionally, peers might interfere within projects in case of a ‘positive-sum game’. Second, interfering is considered the regulators job. Third, Eigen Haard is lacking the information to interfere appropriately. Fourth, Eigen Haard gains status in the stakeholder group when it outperforms peers.

### **Proposition 4: Peers have formal and informal means to intervene**

#### *Few direct means are at hand*

Formally, Eigen Haard has no opportunities to intervene at peers (confidential source). “In general, corporations only discuss with each other in the case of clear positive-sum games. Intervention is way more sensitive. For a start, corporations should start learning of each other” (confidential

citation). However, multiple informal means can be thought of. The informal means can be divided in the direct and indirect means. Directly, Eigen Haard executives might approach the executive board or even the supervisory board of other corporations. Alternatively, the supervisory board of Eigen Haard might approach the supervisory board of the other corporation. However, also because of the arguments in the previous proposition, both alternatives are not put to practice. Contributing to this idea is the notion that ‘if even I, as corporation (i.e. Eigen Haard), know, the supervisory board of the other corporation also knows’. Underlying argument here is that the supervisory board of the respective corporation does have the formal means to secure information, judge on that information and act according to that judgment (confidential source). It is only recently (since the Vestia case and Rochdale affair) corporations may take a look at each other to see how business is going. Still, this is all on a voluntary and cooperative basis (confidential source).

#### *Indirect means are limited by available information*

Concerning the informal and indirect means, peers are capable to approach external regulators as CFV (confidential source). For Eigen Haard, as for pretty much any of the corporations, this informal chatter is “strictly of the record as is sensitive stuff” (confidential source). Topics of this information often concern integrity issues or issues in the internal governance of a peer. Information given is sometimes useful for the external regulator. However, in line with previous propositions, it is often not substantiated and often misses the context of reality. It is the regulator who has to weigh this information, considering it might also be an attempt of a corporation to redirect the regulator focus to a peer (confidential source). Another informal arrangement is chatter between the peers. Peers talk to each other, discussing the performances of others who are not there. Lacking substantiation, this is more considered ‘gossiping’. Also, it does not lead to interventions (confidential source).

#### *Intervention requires stricter norms*

The design of the current system basically does, considering risk taking, not allow anybody (nor peer nor regulator) to act on a judgment. The opportunities provided by law result in the culture and norms of a corporation itself that determine what is acceptable. Eigen Haard is an active, relatively conservative, corporation as well as CFV have barely but their own grounds to judge others on their activities preventively. The question is therefore whether the corporation is questions is organized such a way that it can make its own decisions appropriately. However, this aspect is ignored in current regulation (confidential source). Some corporations themselves require stricter regulation to monitor each other and stricter regulators with more capabilities to intervene (confidential source).

#### *Proposition conclusion*

In conclusion to this proposition, peers have no formal but some informal opportunities to intervene. However, due to the way the system is set up, the sector culture and lacking information, peers are practically only capable of hinting formal external regulators to intervene on other corporations.

### **Proposition 5: Peers have enough degrees of freedom to adjust regulation to the situation at hand**

Peers have practically no means to formally intervene. Informally, there are opportunities, but these are mostly blocked by the sector culture (confidential source). This makes peers dependent on formal regulators like CFV to intervene (confidential source). Peers just being one (and not the most prominent) source of information, it is concluded peers have basically no degrees of freedom to apply regulation according to the situation at hand. Not even considering whether they have insight in the corporation at hand (confidential source).

### 6.3 Woningstichting Geertruidenberg (WSG)

WSG is a smaller sized corporations in the Netherlands (operating around 4.000 vhe) that operates in the Breda region and specialized in care housing. Up until 2010, having the ambition to double in size in just 5 years, the corporation actively bought ground positions. In 2010, this lead to financial problem leading to the current financial restructuring of WSG. A more detailed description of WSG is found in appendix XII. This section further elaborates on the propositions specified to the WSG case.

#### **Proposition 1: Peers have a sense of urgency to regulate one another**

##### *Sense of urgency originates after problems manifested*

The corporations surrounding WSG most definitely have a judgment on WSG (confidential source). For years, corporations surrounding WSG wondered how the relatively small sized corporation WSG was capable to produce so many care housing facilities of high quality. This made surrounding corporations doubt between whether WSG was an example or a threat. This lead to the situation where some peers came to look to study the good example of WSG while others asked questions concerning the risk involved, long term effects etc. (confidential source). However, none of the parties appeared to have any significant insight in nor the activity performance nor the financial performance of WSG (confidential source).

##### *Protection of own position more than regulating the other*

Generally speaking, corporations surrounding WSG discussed the success of WSG (BN DeStem, 2011). It was after that WSG became active in the municipal 'domains of others' and proved to buy ground positions without contracts for development that critiques intensified. However, objective of the critique was not as much as to regulate WSG as to protect the neighboring corporations on position (confidential source). "Corporations always have a negative opinion to other operating in their region. Still, it is extremely rare there is any real substantiation to act upon" (confidential citation).

##### *Proposition conclusion*

In conclusion to this proposition, peers had some sense of urgency to regulate WSG. However, it proves the motivation was more of market protection reasons than WSG risk taking.

#### **Proposition 2: Peers have information about each other's behavior**

##### *Geographical distance to other corporations*

In more rural areas, like the area WSG operates in, regional gatherings are scarce (especially in organized form). A good example is the discussion concerning the income dependent rent. Where in city areas as Eindhoven corporations are aligned (confidential source), in the WSG area peers chose their own policy (confidential source). "In city regions you hear more of your peers. This is trivial as the distances are bigger in rural areas" (confidential citation).

Furthermore, WSG, along with its neighboring corporations, is active in a noncompetitive region. In fact, WSG is the only corporation in Geertruidenberg just as others are the only corporation in 'their' area. This also hampers the information that is available to peers of WSG (confidential source). It is when WSG engages in an activity in a region of a neighboring corporation that this corporations really starts to focus and criticize this WSG activity. A similar action occur when other corporation make an entry into the region (confidential source). "When other corporations engage in the region of a corporation, there are complaints complaints. This is also what mostly explains complaints on WSG" (confidential citation). In both cases, it appears the seated corporation is not having deep insight in the entering corporation (confidential source).

### *No voluntary sharing of information*

WSG is showing its activities, but not the financial result behind these activities to neighboring corporations (confidential source). For example, in showing a successful care housing project focus is given to the quality of the build and the importance of society more than the risk management and financial performance of the project (BN DeStem, 2012a). “In the environment of WSG, corporations doubted how WSG was able to pull this off in terms of risk management. However, on the content, they did not have a clue” (confidential citation). Currently, WSG is in financial restructuring support and information and decisions are much more transparent (confidential source).

### *High cost*

The cost for monitoring peers are immense as there are 389 corporations in the Netherlands. CFV publishes various reports on the performance of corporations (confidential source). However, it is especially the story behind the numbers that is interesting to regulate on. This even further troubles the ability of peers to gather information on one another (confidential source).

### *Proposition conclusion*

In conclusion to this proposition, peers have really limited information of WSG for three reasons. First, in rural areas regional gathering (and, hence, sharing of information) is rare. In rural areas the geographical distinction between corporations is more clear and corporations are more bound to a single municipality (and vice versa). Second, key information was not shared voluntarily. Third, the cost for peers to monitor one another are high.

## **Proposition 3: Peers may interfere with each other's business**

### *Autonomy*

Corporations are autonomous organizations. This makes that neither WSG nor any of its neighbors will interfere in one other's business (confidential source). The financial security structure may raise the expectancy of corporation working together. However, they are separate organizations with separate norms and separate values not appreciating the interference of others. The autonomous value is stronger than the awareness of corporations paying for each other (confidential source).

What the corporations surrounding WSG do have of each other is an opinion (confidential source). They are not afraid of communicating this opinion. However, due to the geographical distinction, opinions of or from WSG can almost never be substantiated by facts (confidential source).

### *Reputation issues*

On the other hand, corporations like when the status of WSG (or its managing director) is damaged, but don't appreciate the spillage of capital it has as a consequence (confidential source). The corporations surrounding WSG are relatively bound to municipalities and don't have real ambition to grow outside this region (confidential source). The financial issues at WSG will require some neighboring corporations to buy units of WSG, thereby limiting their own room for investment (BN DeStem, 2012a). “Originally, other corporations liked Peter Span to get into trouble. Now that WSG is restructuring, nobody says this anymore” (confidential citation). The financial security structure proves not really to motivate corporations to discipline each other. “Corporations know they might have to peer, but they only realize it when we financial restructure a corporation” (confidential citation). Still, interfering in other corporations is considered not done. In fact, corporations in the surrounding of WSG argue regulators are existing to prevent this situation from happening, disqualifying it as an activity they are to undertake (confidential source).

#### *Proposition conclusion*

In conclusion to this proposition, it is not tolerated for peers to intervene at WSG as WSG is an autonomous entity. Moreover, intervening if necessary is a core task of the sector regulators. Also, damaging the status of WSG is considered positive for the own corporation. On the other hand, financial problems at WSG are not appreciated as this may interfere with the investment programs of peers. However, this argument is insufficient in comparison to the others.

#### **Proposition 4: Peers have formal and informal means to intervene**

##### *No formal means*

The means for corporations around WSG to intervene at WSG are limited. Formally, there is nothing peer corporations can do in a direct way. Besides, shown in the previous proposition, interfering in another one's business is not tolerated (confidential source). This reduces the options to the informal and indirect means.

##### *Multiple interdependencies exist to third parties*

In the rural area WSG operates, approaching the municipality of Geertruidenberg seems of no use (BN DeStem, 2012b). WSG is the one of two corporations active in Raamdonkersveer and is strongly connected to the municipality (Confidential source). "The competitiveness in relation to the municipality is not really present there. In fact, WSG did too much for the municipality" (confidential citation). On top, the lack of information on WSG performance makes it unlikely the municipality will act. Also because none of the WSG activities are illegal (confidential source).

##### *Indirect means are limited by available information*

The second option is to approach CFV (confidential source). Before the financial problems of WSG really came to surface, this is what neighboring corporations also did. However, lacking substantiated arguments, it appears neighboring corporations mainly complained on WSG also engaging in their region. It is the individual call of the CFV contact person what to do with this signals as "our methodology was fully focused on numbers" (confidential source). In this judgment, this person has to incorporate more signals that are often more substantiated. Hence, this sets conditions to the usefulness of the mean that are hard for neighboring corporations of WSG to meet because of the geographical distinction (confidential source). However, it is interesting that this mean (though utilized by a person internal in the WSG organization, and, hence, having very specific information) that really brought to life the WSG case. In this respect it is relevant that "relationships with corporations are built with extreme care. Knowing executives longer will lower their barrier to talk of others. Internally, they will only talk on serious integrity violations" (confidential source).

#### *Proposition conclusion*

In conclusion to this proposition, it appears peers have basically no means to intervene. From the sector culture it appears only indirect and informal means can potentially be utilized. However, the characteristics of the rural area WSG operates in make it hard seduce the municipality or CFV into action because of a lack of substantiated arguments.

#### **Proposition 5: Peers have enough degrees of freedom to adjust regulation to the situation at hand**

By the lack of means found in the previous propositions in the WSG case study, this proposition was not discussed. Lacking means, as well as information, it can be concluded that peers don't experience any degrees of freedom to adjust regulation to the situation at hand.

## 6.4 Corporation comparison

This section compares the proposition results from studying the cases of Servatius, Eigen Haard and WSG in order to identify similarities and differences. As such, this section is also structured through the propositions, similar to the other sections in this chapter. Table 6.1 provides an overview of the core notions per proposition for each case.

Table 6.1: Summary of notions for the propositions based on the case study

Proposition	Servatius case	Eigen Haard case	WSG case
<b>1. Peers have a sense of urgency to regulate one another</b>	<ul style="list-style-type: none"> <li>- Lack of precedent</li> <li>- Reputation issues</li> <li>- Vertical disqualifies horizontal</li> </ul>	<ul style="list-style-type: none"> <li>- Lack of precedent</li> <li>- Vertical disqualifies horizontal</li> <li>- Risk dispersion over many peers</li> <li>- Reputation issues</li> </ul>	<ul style="list-style-type: none"> <li>- Sense of urgency originates after problems manifested</li> <li>- Protection of own position more than regulating the other</li> </ul>
<b>2. Peers have information about each other's behavior</b>	<ul style="list-style-type: none"> <li>- Only information of regional peers is gathered</li> <li>- No voluntary sharing of information</li> <li>- Information spread over organizations</li> </ul>	<ul style="list-style-type: none"> <li>- Information is spread over organizations</li> <li>- Internal focus</li> <li>- Only knowledge of 'similar' corporations</li> </ul>	<ul style="list-style-type: none"> <li>- Geographical distance to other corporations</li> <li>- No voluntary sharing of information</li> <li>- High cost</li> </ul>
<b>3. Peers may interfere with each other's business</b>	<ul style="list-style-type: none"> <li>- Autonomy</li> <li>- Reputation issues</li> </ul>	<ul style="list-style-type: none"> <li>- Autonomy</li> <li>- Vertical disqualifies horizontal</li> <li>- Interference requires deep knowledge</li> <li>- Reputation issues</li> </ul>	<ul style="list-style-type: none"> <li>- Autonomy</li> <li>- Reputation issues</li> </ul>
<b>4. Peers have formal and informal means to intervene</b>	<ul style="list-style-type: none"> <li>- Lack of effective direct means</li> <li>- Third parties provide means to discipline peers</li> <li>- Peers approach regulators only informally</li> </ul>	<ul style="list-style-type: none"> <li>- Few direct means are at hand</li> <li>- Indirect means are limited by available information</li> <li>- Intervention requires stricter norms</li> </ul>	<ul style="list-style-type: none"> <li>- No formal means</li> <li>- Multiple interdependencies exist to third parties</li> <li>- Indirect means are limited by available information</li> </ul>
<b>5. Peers have enough degrees of freedom to adjust regulation to the situation at hand</b>	<ul style="list-style-type: none"> <li>- High barriers to overcome</li> </ul>	<ul style="list-style-type: none"> <li>- Practically none</li> </ul>	<ul style="list-style-type: none"> <li>-</li> </ul>

### Proposition 1: Peers have a sense of urgency to regulate one another

Over all three cases studied, corporations knew that the potentially had to pay for one another. However, it proved corporations only became painfully aware after Vestia case. Before the Vestia case, there has been one claim on the security structures due to corporation mismanagement. Even now corporations are aware, it appears a real sense of urgency is lacking. In studying the cases, a variety of reasons is named on top of this 'burden of history'.

In all three cases, the existence of formal regulators is a relevant concept. In striving to be better than the other, it is not really undesirable when the peer is bleeding as long as it does not hamper

your own organization. The other way around, strive for status allows risk taking between peers. It is the core task of the formal regulators to set boundaries and define what is acceptable and what is not.

Furthermore, it appears that opinions on one another are bound to the own area of activities. This is made clear especially in the case of WSG, where peer corporations started forming opinions of WSG when WSG became active in their traditional regions of activity. In all three cases, it proved opinions are also based more on 'whining pub talk' more than factual information.

Finally, in all three cases it appeared the market conditions made corporations 'lazy' in regulating one another though for various reasons. In the case of WSG, operating in a more rural area, corporations act geographically quite distinct making there is no real competition between corporations. In the case of the more urban operating corporations of Servatius and Eigen Haard, market pressures reduced the need for controlling peers. The market pressures are high, so that barely any vacancy in social housing units in (at that time) good economic conditions with rising real estate values. Hence, this might have set the conditions for the 'lack of precedent' to exist.

### **Proposition 2: Peers have information about each other's behavior**

From the individual cases, it follows corporations do have some information on peers they can compare themselves with. Maastricht corporations know Servatius engaged in, amongst others, the campus project and the Lambertuskerk. Eigen Haard has some knowledge on the activities of the Amsterdam corporations in Amsterdam and vice versa. Corporations neighboring WSG knew activities of WSG to some extent. However, in all cases, it appears only basic (i.e. publically accessible) knowledge on activities was present. There appears to be little knowledge on the financial performance of the activity as well as the (financial) performance of the corporation as a whole. This information is considered strategically valuable and therefore not shared voluntarily.

The information peers do have of each other appears to be based more on interaction than on facts. In that respect it is interesting to see that Servatius and Eigen Haard, urban corporations who participate in regional gatherings, appear to know more of their peers than WSG (and vice versa), a rural corporation. Being a rural corporation, WSG operates in a more geographically demarcated area. Becoming active in the habitat of a peer (or vice versa) proved to be a motivation for some basic monitoring of activities.

Concerning information on the financial performance, all cases show corporations use less information than is publically available. Each year, CFV publishes CiP reports, benchmarking a corporation's performance in respect to its geographical peers and peers in activity type. Corporations barely take notion of their peer performance from these CiP reports as well as study year reports of corporations themselves.

Furthermore, demonstrated in the previous proposition, it proves none of the corporations is interested in regulating one another. Corporations mirror themselves to somewhat comparable peers. This proves to be for status issues, making most corporations benchmark themselves on a regional level and only the very big (like Ymere and Alliantie in the Amsterdam region) benchmark themselves more on a nationwide level. Financial aspects do not prove to be as relevant as are the 'crown-jewel' activities. This also contributes to corporation protecting their information and sharing information to peers in a select way.



Since the Vestia case, corporations start monitoring one another more closely. They share more information with each other, though this is more done for the purpose of learning of one another than monitoring one another. The level to which information is shared is very different per region. Still, the increase in information sharing is a positive development for the functioning of peer monitoring.

### **Proposition 3: Peers may interfere with each other's business**

Corporations don't allow for others to intervene and consider it not-done to intervene at others. Each organization is a separate autonomous organization with its own values and norms. This makes that intervening on each other is simply not done. The lack of means to intervene (next proposition) may further contribute to this feeling.

Furthermore, corporations are battling for relative status for one another. For the willingness to interfere at one another, this has multiple consequences. In the battle for status, it is accepted for peers to engage in non-DAEB 'prestige' activities. In general these non-DAEB activities are riskier but contribute to status more than a DAEB activity as the restructuring of 200 housing units. The campus project and Lambertuskerk are examples for Servatius. Eigen Haard engaged in projects like Fountainhead and New Kit. And, although DAEB activity, WSG heavily engaged in high quality care housing. Any of these projects lead to significant amount of press releases, thereby potentially being a good indicator for status impact of these projects.

So, peers allow themselves to take on more risk than strictly necessary. In this respect, it is also useful for peers when other fail (i.e. 'bleed') in these projects as in indirectly raises their own status. The limit is reached when corporations experience disadvantages themselves of another corporations risk taking. This not always requires the financial restructuring fund. For covering the losses of the Campus project, Servatius is selling a lot of property disturbing the local market. This local market includes the projected selling of housing units by the other corporations. In case of WSG, neighboring corporations will have to buy some of WSG property which, if at all present in their working areas, hampers their investment capability. However, peers allow for each other to take on risk as a formal regulator (i.e. CFV) is existing to limit that risk.

Furthermore, CFV district advisors argue that interfering requires deep knowledge of the corporation that is unavailable to the peers. In that respect it appears are mostly either missing the core of problems or missing some significant nuances (also see proposition 2 in this respect), making it basically impossible for peers to intervene effectively.

### **Proposition 4: Peers have the formal and informal means to intervene**

In each case, it appears peers have no formal means to intervene at each other. On top, proposition three argued the direct informal means are not tolerated. There are two indirect and informal means corporations may make use of: approaching the municipality or CFV. Utilizing this means is often hard as corporations are interdependent to these organizations and each other in multiple ways.

Since the Vestia case, corporations start discussing their opportunities to intervene more open. Still, no formal means are identified on large scales, but corporations are more open to best practices of other corporations. Also, these other corporations are found to be more willing to help (i.e.

‘intervene’) at others. Although these arrangements all function on a voluntary basis, making it relatively easy for corporations to distance themselves from peers, it are these subtle mechanisms that start to function better.

The municipality is to have performance contracts with the corporation in its region. Through this contracts it binds corporations to municipality plans on the development of housing in the region. An indicator for financial issues might be a corporation not realizing this agreement. If peers suspect a corporation is not able to live up to the contract they potentially may approach the municipality that can then start a deeper investigation. However, it appears the performance contracts also have some limitations in practice. In the Maastricht region these contracts are present. The municipality of Amsterdam does not seem to work with detailed performance contracts as much. Geertruidenberg has a one on one relation with WSG, reducing the opportunities for peers to intervene here. Hence, for peer monitoring on the financial performance of corporations, this mean does not seem directly effective.

The second approach is peers stepping up to the formal regulator, CFV. It proved this mean is so sensitive, it is strictly utilized ‘off the record’. Hence, the relation between the corporation and the DA is very relevant for retrieving information from peers. However, already discussed in proposition 2, peers are limited in the fact based information they have on each other. The notion of peers worrying on each other, especially if it concern multiple peers on the same reason, it might be an incentive for the DA to research on these concerns.

Second limitation of approaching CFV is that, in practice, it is often CFV who approaches the corporation. In all cases, it is strictly that during a ‘regular’ visit of CFV to a corporation the topic of peers might come up in the margin of the conversation. This imposes some significant delays as a DA has a conversation visits a corporation only once a year. The barrier for the corporation to actively approach CFV proves too high. Therefore, even when corporation have significant this mean might be ineffective as thing may turn bad within a year (for example the Servatius campus project).

**Proposition 5: Peers have enough degrees of freedom to adjust regulation to the situation at hand**

Corporations have a really limited arsenal of means to intervene, both formally and informally. Furthermore, the culture and drive for status limit the usability of these means even further. Therefore, even though some degrees of freedom on the means to intervene are present, barriers to utilize seem to be so high that peer regulation cannot be considered responsive.

## 7. Proposition findings

Based on the institutional analysis (chapter 5) and the case study (chapter 6), this chapter evaluates the propositions identified in chapter 3. The discussion on propositions in the first section of this chapter provides a clear overview of the ability and willingness of peers to regulate one another. This leads to an overall insight of peer monitoring functioning that is discussed in the second section. The third section concludes this chapter by discussing the consequences of peer monitoring arrangement in the Dutch housing sector for moral hazard in that sector.

### 7.1 Proposition results

This first section brings together the case study and institutional analysis to evaluate the propositions identified in the beginning of this research. The five identified propositions were formulated as follows:

- Peers have a sense of urgency to regulate one another
- Peers have information about each other's behaviour
- Peers may interfere with each other's business
- Peers have formal and informal means to intervene
- Peers have enough degrees of freedom to adjust regulation to the situation at hand

#### 7.1.1 Peers have no sense of urgency to regulate one another

Peers prove to have no sense of urgency to regulate one another. Although corporations know they potentially have to pay for each other, the awareness of this risk lowered through rising real estate values and favourable economic conditions. No significant claim on the security structure has been made before 2010, also not concerning the governmental security structures in place before the autonomization of the sector in the 1990s.

The hybrid concept of the sector, i.e. private organization fulfilling public goals, makes corporations competitive but no real competitors. In practice, this means missteps of corporations are favourable for peers as long as it doesn't hamper their own activities (competitive) but there is no market function to bring real consequences to the missteps (no competitors). Corporations don't feel to discipline each other from their competitive setting and with formal regulators existing whose core task is to prevent (excessive) bleeding of corporations. Since 2010, this perception somewhat changed. Peers now cooperate more with each other. Still, this cooperation is on a voluntary basis.

Finally, peers also miss ground to regulate one another as there are many freedoms to engage in risk. By current legislation, many activities of corporations can be legalized. Hence, there are wide possibilities to take on risky activities. This is supplemented by the easy conditions from which corporations can finance themselves. The government backing in the security structures provides corporations with cheap and loans.

#### 7.1.2 Peers have only little information about each other's behaviour

Peers lack the formal means to gather information of each other. Hence, they are dependent on the information shared by peers. As peers are competitive, especially before 2010, no information was shared voluntarily. On top, gathering information of peers is costly as there are 388 of them across the Netherlands. Currently, corporations start sharing information more.

In the context of the peer arrangements, the geographical distance of peers is relevant. Corporations typically operate in a specific region. In this region they have some awareness of their peers, though more on engagement in activities than financial performance or risk management. This imposes extra barriers on a corporation being informed on its 388 peers.

### **7.1.3 Peers won't interfere with each other's business**

Peers have become autonomous organizations quite recently, and don't tolerate other corporations to interfere nor will they interfere on another corporation. There is no real willingness to set aside these norms as regulators are existing that have more information and are dedicated to preventing security structures to be used. Furthermore, the autonomy of corporations is backed by the concept that in their drive for status, corporations allow peers to bleed as long as it has no consequences for themselves. Again, it is (considered) the task of regulators to limit this 'bleeding'. Finally, corporations are interdependent in a number of different way. In protecting their relationships in for example project development, corporations won't easily interfere to each other.

These barriers are in addition to a barrier in the security structure itself, being that risks are dispersed nationally. The spreading of negative consequences over all peers makes that the damage for peers is relatively low. Hence, these limited downsides in respect to the gains from the financial security structure don't provide a real incentive to interfere. Again the Vestia case is the exception that causes peers to discuss this issue more actively. Since Vestia, subtle mechanisms for peers to interfere start to develop

### **7.1.4 Peers have limited formal and informal means to intervene effectively**

As a formal means, peers may use the integrity hotline of BZK to report integrity issues at corporations. The formal opportunities of Aedes to discipline peers seem limited to use for a single peer. Aedes measures generally are to be applied to all members, thereby slowing down decision making significantly. Peers do not recognize both of these formal means as intervening at one another is not done. Apart from the formal means, this also holds for the informal but direct means also because missteps of others are beneficial to the relative status of a corporation.

This leaves the informal and indirect means to intervene, two of which are distinguished. Peers may utilize the performance contracts municipalities are supposed to have with corporations. However, the possibility to use this arrangement basically seems to depend on the extent to which municipalities use these contracts and the municipal context, e.g. whether there are multiple corporations active in the municipality or not.

The second informal and indirect means is to approach CFV. In practice this possibility is utilized, although practically it is CFV who visits/approaches a peer for regular visits. In these visits corporations may discuss their peers off the record. It proves this arrangement is only partly effective as a corporation standard only has a single visit of CFV per year causing delays. Furthermore, already discussed in the previous propositions, it proves corporations often have little information on their peers. DAs of CFV obviously receive more signals than just of peers, making substantiation and the relation with the DA important for the effectiveness of the arrangement.

### 7.1.5 Peers have no degrees of freedom to adjust regulation to the situation at hand

The limited arsenal corporations have is limited by institutional burdens in place. These institutional burdens prevent peers from utilizing direct and indirect formal means. The real internal focus of corporations and their autonomy also make that direct informal means are not appreciated either. This leaves just few indirect and informal means for corporations to discipline their peers.

In using indirect means (especially when they also are informal), corporations also lose a lot in the sensitivity of the effect of their judgment. Other organizations, mostly regulators, pick up these signals and interpret them in their own way. Hence, the responsiveness of corporations in disciplining their peers is really limited. Already lacking the basic conditions for peer monitoring to function as an effective regulator, the responsiveness is no longer considered in the remainder of this research.

## 7.2 The potential of peer monitoring in the Dutch social housing sector

The overview of the proposition shows interdependencies between the propositions. The four propositions were categorized by differentiating the regulator activities on willingness and ability (section 3.5). In table 7.1, the proposition findings are summarized. Based on the proposition results discussed in the previous section, this section generalizes this finding to the capability and ability of peers to monitor one another and their responsiveness in monitoring each other. The elements represented in italic in figure 7.1 directly result from the peer monitoring arrangements, others are dependent more on the context peer monitoring operates in.

Table 7.1: Summary of proposition results

	Willingness	Ability
<b>Director</b>	Low, because: <ul style="list-style-type: none"> <li>· Competitiveness</li> <li>· Lack of precedent</li> <li>· Formal regulators exist</li> <li>· Freedom to engage in risk</li> </ul>	
<b>Detector</b>		Low, because: <ul style="list-style-type: none"> <li>· <i>No voluntary sharing</i></li> <li>· <i>Many peers: costly</i></li> <li>· Geographic distance</li> </ul>
<b>Effector</b>	Low, because: <ul style="list-style-type: none"> <li>· <i>Many peers: 'low' risk</i></li> <li>· Competitiveness</li> <li>· Mutual interdependencies</li> <li>· Autonomy of organization</li> <li>· Formal regulators exist</li> </ul>	Low, because: <ul style="list-style-type: none"> <li>· <i>Few direct means</i></li> <li>· Formal indirect means not recognized</li> <li>· Dependent of others for Indirect informal means</li> </ul>

### 7.2.1 Peers have a low willingness to monitor one another

Even though peers are supportive to each other in financial terms, peers have a low willingness to monitor each other, even though peers are supportive to each other in financial terms. This is directly related to the fact that risk is dispersed nationally (i.e. over 389 peers) and few significant cases occurred before 2010. Furthermore corporations are competitive to each other, though this is slightly changing since 2010. Also in the context of the arrangement, peers are interdependent in other ways than risk sharing, for example in relations to the municipality or combined projects. This

further limits their willingness. Furthermore, corporations are autonomous organizations that experience many freedoms to take on risk while formal regulators are in place to monitor the corporations.

Since three years, the willingness to be aware of the activities of one another has increased together with the willingness to cooperate. The willingness to interfere to the other is still very low, also because of the low ability to interfere at others, see paragraph 7.2.2.

### **7.2.2 Peers have a low capability to monitor one another**

Peers have no means to secure information and corporations don't generally share information voluntarily. Since 2010, this is somewhat changing as the mindset of corporations is changing from competitiveness to collaboration. Still, corporations use less information than publically available. The monitoring of peers is a complex and costly activity not directly contributing to a corporation's core. The geographical distance also hardens it, as nearly all corporations are active in distinct regions. Furthermore, peers also lack the ability to discipline one another. Few direct means are available. Also in the context, formal means are barely present and direct means are not tolerated. This makes that corporations basically only can sanction peers through regulators they approach in an informal way. The effectiveness of these approaches is seriously doubted, amongst others because the poor information corporation can substantiate their opinion with and the delay involved in this sanctioning mechanisms.

### **7.2.3 Peer monitoring may well have potential, though it has not functioned in the past**

Lacking the ability and willingness of peers to monitor one another, peer monitoring proved not to be as effective as peer monitoring theory suggests. The sharing of risk provides a strong incentive to monitor one another when risks materialize. However, this incentive is weakened as risk is shared over many peers and cost of monitoring all peers is high. Context factors also reduce the willingness of peer to monitor one another. On top, peers lack means to discipline each other. This suggests that peer monitoring has no potential to manage moral hazard.

However, the willingness proves to change over time. Because of the economic downturn and the Vestia case, the willingness of peers to monitor one another has significantly increased since 2010. This also implies the importance of context factors influencing the effectiveness of peer monitoring. Very subtle mechanisms of peer monitoring now start to function from which peers are in a better position to gather information and discipline one another. Further professionalization may reduce current barriers further, making peer monitoring more effective in managing moral hazard. This also requires some institutional arrangements to change (studied in chapter 9). Hence, peer monitoring may have potential in managing moral hazard.

According to literature, the core strength of peer monitoring is the smaller asymmetry in information peers have in comparison to vertical regulators, especially in giving knowledge to information. Precondition for this is peers having information of one another. As this is currently not the case, not much can be said with regard to this notion.

### 7.3 Consequences for managing moral hazard

Chapter 3 explained the core conditions of moral hazard to be asymmetric information and conflicting goals. The idea that peers have and use similar knowledge and expertise to discipline each other, i.e. peer monitoring, was argued to have the potential to mitigate these conditions. Sharing the consequences of risks taken when they turn out bad was thought to provide the willingness for peers to monitor one another.

However, as section 7.2 summarizes, peer monitoring does not necessarily fulfill these conditions. Not willing to regulate one another and not having more information than formal regulators, peer monitoring arrangements as implemented in the Dutch social housing sector have a low effectiveness in managing moral hazard. Recent developments in the context indicate peer monitoring has some potential in managing moral, but arrangements are underdeveloped. Further professionalization of peer arrangements may well prove the full potential of peer monitoring in managing moral hazard.

Peer monitoring is not the indisputable way to go in limiting the negative effects of moral hazard. However, the involvement of peers is a good way to protect the positive effects of moral hazard whilst limiting the negative effects of it. Still, other possibilities to manage moral hazard besides peer monitoring exist. Suggestions on these alternatives are discussed in chapter 10.



## 8. Validity

In section 4.9, the validity of this research was introduced. Three concepts proved particular relevant: construct validity, external validity and reliability. This section discusses the ‘performance’ of this research on each of these subjects. It was already noted validity is an ambiguous factor representing ‘trust’ in the findings of the research. As such, this chapter is an evidence file identifying limitations.

### 8.1 Construct validity

The construct validity focusses on the correct establishment of operational measures for the concept of study. Yin (1989) identifies three tactics for increasing construct validity: use multiple sources of evidence, establishment of a chain of evidence and a report review by key informants.

This research respects the first two tactics by having two analysis complementary to one another: the institutional analysis (mainly build on documents and archives) and the case study (mainly build on interviews). Interviews were held with both regulators as well as corporations (as mentioned in chapter 4). These interviews concerned multiple cases. Studying multiple cases contributes to the chain of evidence as well as to the external validity discussed in the next section.

### 8.2 External validity

External validity deals with the issue of knowing whether case study findings are (analytically) generalizable beyond the studied cases. This issue is closely related to the amount of replications. As this research studies only 3 out of 389 corporations, the generalizability of the results to the sector and thereafter can be doubted. Most definitely, supporting research is needed for the findings to result in general applicable theory. However, concerning the Dutch social housing sector, the external validity seems quite good.

Much attention was given to the case selection. Limited by resources, only three cases could be studied. Still, the three cases studied were distinctly different corporations in terms of (financial) performance, size, geographic location, demographic developments and activity specializations. As much as possible, the three cases are representative to the sector. From the interviews, two particular cases arose interesting in cross checking the findings of this study.

The first is that of a regional gathering of corporations in the northern part of the Friesland province. With public information on financial performance available, these corporations benchmarked each other. Furthermore, he argued these corporations got into a fight on what is good what is not and they won’t tolerate each other’s comments. In the end, this led to multiple corporations withdrawing themselves from the gathering membership. As such, this exception also confirms many other findings.

A second example is that of the “Lichttoren” project in Eindhoven. The Lichttoren project was initiated by a project developer that actively tried to sell it to corporations. None of the corporations engaged in the projects, but the developer kept on trying. In the end, the Trudo corporations was convinced and started developing the project. This made other corporations to grump as they are convinced of the project not being feasible. So, there was some form of peers monitoring one another. However, the project had to be (and was) approved by BZK for Trudo to start investing. Before this approval, no corporation complained. It is only after the regulatory procedure corporations started complaining (confidential statement). Currently, 4 years later, the project is largely developed. Initially the project performed relatively well. It is only recently some minor

depreciations are made on the Lichttoren project (Trudo, 2012). So in this project corporation did somewhat monitor their peers. However, they started communicating their doubts only after the official decision making. Their doubts were only based on up front knowledge, not being informed on the latest information. It is still questionable 'who is right'. Still, this form of monitoring is considered unique (confidential statement).

### **8.3 Reliability**

The reliability aspect concerns whether the same results are produced if the same procedures are followed. Two elements in particular contribute to the reliability of a case study (Yin, 1989). First, the use of a case study protocol. The case studies are structure by the propositions identified in chapter three. These propositions form the basis for the analysis. The protocols for the interviews (both the questions and points of attention) are included in the appendices of this research. Furthermore, the report is set up in such a way that an external researcher should be able to examine (and, more important, repeat) the research process from the research questions all to the conclusions.

Second, an evidentiary base on which the findings are based contributes to the reliability. The written documents are all non-confidential and can be found through the reference list included to this research. From some documents a subscription may be required. Manuscripts of the interviews are included in the appendices. In text there is consistently referenced to the corresponding sources of information when making claims. As such, this research is considered repeatable and therefore reliable.



A detailed architectural drawing of a building facade is shown, featuring a curved wall with windows and a door. The drawing is overlaid with a red semi-transparent rectangle containing the text 'Part III – Improvement'. Various drafting tools are present: a yellow spirit level with a green bubble, a black ruler, a yellow ruler, and a black pencil. The drawing includes labels such as '212' in a window, '218' in a door, and 'PER BATTEN ROOF' near the roofline. The background of the drawing shows a stone wall and a hatched pattern.

## Part III – Improvement



## 9. Alternatives for improving peer monitoring in the sector

In its current form, peer monitoring is not effective in managing moral hazard in the Dutch social housing sector. Shortcomings in both willingness and ability hamper peers in successfully performing the regulatory tasks, i.e. effectively regulating each other. This chapter discusses alternatives that improve the functioning of peer monitoring in Dutch social housing by reducing the barrier identified in the analysis. Only alternatives that directly relate to peer monitoring are considered. The first section structures the discussion on alternatives in the other sections of this chapter.

### 9.1 Chapter structure

In discussing the analysis results, multiple barriers were identified that hampered the effectiveness of peer monitoring in managing moral hazard. These barrier were presented in table 7.1. Some of the factors directly result from the set-up of the peer monitoring arrangements. Other barriers are dependent more on the context peer monitoring operates in. In the remaining sections of this chapter, alternatives are presented to reduce these barriers. For that reason, a distinction is made between barriers on the willingness or ability. Second, a distinction is made to barriers on the peer monitoring arrangement or the context of the arrangement (table 9.1). Section 9.2 discusses improvements to mitigate barriers in willingness from the current arrangements. Section 9.3 does this for the ability barriers. Improvements to limit context barriers on the willingness are discussed in the section 9.4 before discussing context barriers limiting the ability in the section 9.5. Section 9.6 provides the conclusions of this chapter.

Table 9.1: Barrier categorization in this chapter

	Willingness	Ability
Peer monitoring arrangement	<b>Section 9.2:</b> <ul style="list-style-type: none"><li>- Many peers: 'low' risk</li></ul>	<b>Section 9.3:</b> <ul style="list-style-type: none"><li>- No voluntary sharing</li><li>- Many peers: costly</li><li>- Few direct means</li></ul>
Peer monitoring context	<b>Section 9.4:</b> <ul style="list-style-type: none"><li>- Competitiveness</li><li>- Lack of precedent</li><li>- Formal regulators</li><li>- Autonomy of organization</li><li>- Mutual interdependencies</li><li>- Freedom to engage in risk</li></ul>	<b>Section 9.5:</b> <ul style="list-style-type: none"><li>- Geographic distance</li><li>- Formal indirect means not recognized</li><li>- Dependent of others for indirect informal means</li></ul>

### 9.2 Reduce arrangement barriers on the willingness of peers

From the analysis, only a single barrier is identified that limited the willingness from within the arrangement: The sharing of risk over many peers lowers the impact for peers. Hence, it lowers the incentive to monitor one another. This section suggests improvements to the arrangement to lower this barrier.

The contributions on the financial restructuring of others hurts, but does not directly threaten the existence of the contributing corporation. Though it is important to not get a 'domino of casualties', the current situation does not fully incentivize corporations to regulate on their peers. Several alternatives are thought of for strengthening this incentive (table 9.2).

Table 9.2: Alternatives to increase damage for peers to incentivize peer monitoring

No.	Alternative
1	Specify financial restructuring contributions on more than corporation size
2	Assign maximum facilitation volumes to groups of corporations
3	Adept corporation ownership structure

### 1. *Specify financial restructuring contributions on more than size*

Currently, the corporation contribution to the financial restructuring funds of CFV is based on the size of corporations. This is suboptimal for peer to monitor one another as a large corporation in the Randstad area might have to pay relatively much for the problems of a small corporation in the Groningen area it has never even heard of. As corporations mainly mirror themselves on their geographic peers of equal size, geographic distance might be a relevant aspect to include in the division of cost. An example of a specific parameter might be the distance between the headquarters of corporations and corporation turnover.

Another relevant aspect to specify the financial contribution on is the type of activities, e.g. student housing corporations pay for each other, just as care housing corporations do. This may bring this corporations closer together. Alternatively, corporations may choose their own groups. This will bring the corporations together that already are closer together, i.e. have a relative good sense of one others performance and risk preference (Stiglitz, 1990). When the potential contribution is significant enough, it will also transition the peer behavior more from ‘mirroring’ to ‘monitoring’.

An obvious downside of this alternative is that in the case financial restructuring report is needed for one of the corporations, similar corporations carry (a significant part of) the cost. However, it could well be these corporations are specifically needed to support the corporation in other ways as well (e.g. by the buying of equity of the corporation).

### 2. *Assign maximum facilitation volumes to groups of corporations*

Based on a categorization of corporation by regulators (e.g. based on a mixture of size, geographic location, activity pattern, financial performance) or corporations themselves (on their own preference), these facilitation volumes could be assigned to small groups of corporations, although still needing a division between corporations in the group. When a corporation’s facilitation volume is part of the facilitation volume of a group, financial issues at a corporation directly influences the investment strength of peers. In other words, it directly ‘sanctions’ the peer for not effectively monitoring the corporation. This increases the willingness to monitor each other. Simultaneously, peers are better able to monitor because of the small and clear demarcation in peer groups.

Core condition is that a corporation is also capable of sanctioning its peers. The downside of this alternative is that a corporation might require some extra investment opportunities in case of financial issues at a peer in order to protect region stability.

### 3. *Change corporation ownership structure*

Being social enterprises, corporations have no clear owner. This takes away incentives for corporations to work efficiently as they have no demand on returns (Hoekstra, Hoogduin, & Schaar, 2012). This is not easily mitigated as capital is not allowed to leak outside the sector.

However, this directly gives potential for improving peer monitoring in the sector. Corporations may be shareholders of one another. Shares can be divided on the basis of corporation size, or more on the peer groups as is demonstrated in other alternatives. Through the shareholder structure, corporation may have to pay for the losses of a corporation but also gain from a well performing corporation. There are three main advantages. First, corporations experience the performance of their peers on a structural i.e. yearly basis. Second, corporations may also benefit from the good performance of another corporation instead of only be punished. Third, when this demarcated market structure allows for the trading of shares, share values are potential indicators for regulators to focus on specific corporations without corporations explicitly having to sell each other.

Downside of this approach is that good in the short term may proof bad in the long term. For example, take the Vestia case where corporations seemed to be benefitting from derivatives and losing the corresponding risk profile. To mitigate this downside some options are available. Think for example of the regulators (or national government) having a majority share or preference shares enabling then to gentle steer a corporations heading without formally intervening.

9.3 Reduce arrangement barriers on the abilities of peers

From the analysis, three barriers are identified that limited the willingness from within the peer monitoring arrangement. First, peers don’t share information voluntary. Second, the ability to gather information is limited as information gathering is costly due to the many peers. These two topics are discussed in the first paragraph of this section. Third, peers lack means to intervene to one another. This is covered in the second paragraph of this section.

9.3.1 Enable peers to gather information

For a corporation it is practically impossible (or, at best, immense costly) to be informed on the behavior of all its 388 peers. The effort of monitoring each other will basically decrease linearly to the decreasing amount of peers a corporation has to monitor. So, limiting the size of groups will lower the cost of gathering information. In section 9.2, opportunities were already presented to limit the group size. This paragraph further focusses on the sharing of information over peers (table 9.3). Alternative 2 to 4 focus on context improvements to improve the mitigate barriers within the arrangement.

Table 9.3: Alternatives to increase the ability of peers to gather information

No.	Alternative
1	Formalize peers sharing information
2	Enhance public available information from regulators
3	Increase interdependencies between peers
4	Enhance information from ‘lighthouses’

1. Formalize peers sharing information

Currently, peers don’t have the formal ability to gather information from each other. Hence, peers are dependent on the willingness of a corporation to share information. From the analysis, it proved they barely do so voluntarily. Formalizing the ability for peers to gather information can be done through legislation, regulatory procedures or branch organizations like Aedes. Important in this respect is who will share information to whom to prevent an overload of information. It is also questionable what information is to be shared. One way or the other, this will require some form of centralization.



### *2. Enhance public available information from regulators*

Every year, CFV publishes CiP reports. These reports contain quite specific information on the performance of individual corporations. Only the reports are public, the underlying database is not. When the database is publically available, software can be used to automatically and quickly set up comparisons between corporations of interest. This will lower the barrier to be informed on peers and makes the sector more transparent.

### *3. Increase the interdependencies between peers*

Peers currently gather in ad-hoc networks. Often, these are regionally oriented. Peers in these networks are generally better informed on one another. Corporations participate in these networks because of some sort of interdependency to the other corporations in the network. This could be the realization of performance contract to the municipality, but also on commercial project development or knowledge sharing on information like derivatives.

Generally, the stronger the interdependencies, the more information is shared. Hence, creating stronger interdependencies might give the ability to peers to be better informed of each other. These interdependencies can be created by peers themselves, but also by third parties. For example, through the performance contracts of the municipality. The withdrawal or non-participation of a corporation in such a group might provide a signal in itself (confidential source) towards regulators. A downside to this alternative is that stronger (tangible) interdependencies also potentially leads to an increase in moral hazard behavior. Furthermore, interdependencies between peers was considered a barrier in itself. This is further elaborated on in section 9.4.

### *4. Enhance information from 'lighthouses'*

More organizations, like municipalities, are active in the Dutch social housing sector than just corporations and regulators. These third parties might function as lighthouses, i.e. provide warnings, on sector developments. An increase in transparency from these third parties enables peers to know more of each other. Besides, it also helps the lighthouses to perform their function better. Limitation is that some lighthouses also have other interest, making the information valuable. For example, a municipality is also willing to sell ground to corporations. As such, it more or less motivates corporations to take on risk (i.e. pay a higher price) and is not willing to share that information to other peers. Others, like VTW and NVBW, have less of these conflicting interests.

#### **9.3.2 Enable peers to intervene**

Peers currently are in no formal position to sanction one another. So, though there is a mutual relation through the security structures, there is no mutual possibility to discipline one another. Most straightforward, these possibilities (for example like regulators have them now) to impose on one another may be established by legislation, through regulators, or through peer organizations like Aedes. In all of these cases, it is highly likely some form of centralization is needed to sanction peers as long as risk is shared over many peers.

There is, however, also an organizational change that inherently brings options to discipline on another: making corporations shareholder of each other. This way, corporations have better insight and can have legal means to discipline one another through a corporation's statutes. This option was already elaborated on in section 9.2.

Giving peers the opportunity to sanction one another has at least one big weakness. Peers are interdependent in multiple ways. This, in combination with group sanctions, hampers peers disciplining one another. This is seen in many other sectors as well, like the European Union (Porte, 2002) and the United Nations (Greif, Milgrom, & Weingast, 1994). Corporations work with each other on multiple projects for longer periods of time. This makes the relations between corporations very important in respect to the unsure event of a corporation making a claim on the financial security structure as peers will have to work with each other in the future. In other words, the relation of peers is characterized by reciprocity and repetitiveness, making it harder for peers to intervene.

## 9.4 Reduce context barriers on the willingness of peers

From the analysis, six barriers in the context of the peer arrangement are identified that limit the willingness of peers to monitor one another: competitiveness, lack of precedent, existence of formal regulators, autonomy of corporations, mutual interdependencies and freedoms to engage in risk sharing. Apart from the autonomy of corporations and freedoms to engage in risk sharing, alternatives for each barrier are discussed below (table 9.4). Alternatives on the freedoms corporations experience in their risk taking is elaborated in chapter 10.

Table 9.4: Alternatives to reduce context barriers on the willingness of peers

No.	Alternative
1	Choose between colleague or competitor
2	Increase amount of claims on security structure
3	Use the existence of formal regulators
4	Utilize interdependencies between peers

### 9.4.1 Choose between colleague and competitor

Being social enterprises, corporations are competitive to each other (as they are private organization) without being competitors (as they serve the same public goal). As such, peers are in a vague position in monitoring corporations as they together have to fulfill the social housing objectives of a municipality while they like each other to bleed as they are competitive. Making this relation tilt to corporations experiencing each other either as colleagues or as competitors provides two alternatives that improve both the willingness and ability of peer monitoring in the sector. Both alternatives also provide opportunities from a network context. These opportunities are further elaborated on in section 10.4.

Peer monitoring will be incentivized when corporations feel themselves bound more to the public goal they are to fulfill together. In this respect, smaller group of corporations may be of great contribution as corporations work together in geographical distinct areas to realize the social housing objectives of the municipality. Therefore, cooperation with other organizations may prove helpful in managing each other's behavior. For example, performance contracts of municipalities playing a stronger role in peer performance evaluations. Or adding risk taking and financial performance to the agenda of the regional gatherings of corporations. This would require to allow the regional gathering to grow in strength. VNG is an example in the banking sector where voluntary gathering proved capable to have significant power to influence banking behavior (Bekkers B. , 2002). A third alternative in this respect is to reduce non-DAEB activities of corporations. It is often these activities that risks are taken and materialize. It is also the field where corporations are competitive most.

The other option, making corporations more competitors of each other, in most cases will limit the role of peer monitoring in the sector. In some cases, it might be beneficial though. Think of tendering procedures for example. Currently, procedures are open for anybody to subscribe but the resulting contract is often confidential. If this information is given to peers, peers are able to test the bid of the winning party against the market.

#### **9.4.2 Increase the amount of claims on the security structures by sharing losses in BMV**

Currently, corporations only pay for each other in the case of financial restructuring at a peer. These contributions are quite rare. However, more corporations take losses in their social capital (BMV) but are able to level on these losses internally. In sharing on the losses in the individual projects corporations have to pay more frequent for each other, without extra loss of social capital. Spreading loss of social capital over peers makes corporations more 'social' to each other. In paying more frequent for one another, the awareness and willingness to monitor each other closer will rise.

As a downside, this measure potentially increases the moral hazard. When for each loss in each project peers support each other, the incentive for the corporation itself to take on risk grows. A limitation of the alternative it is hard to identify losses on individual DAEB projects, as these projects are not profitable by themselves. For non-DAEB projects the identification of losses is easier, as it is expected the projects are profitable.

#### **9.4.3 Use the existence of formal regulators**

The existence of regulators limits the willingness for peers to monitor one another. Peers currently don't have a formal role in regulatory procedures. However, peers may play a significant role in managing moral hazard through regulators. Peers see each other more often and are better capable to give knowledge to information (confidential sources). One of the problems in regulating moral hazard is that risks only materialize after they are taken and activities are generally not (or barely) reversibly. This makes that 1) both peers and regulators are always lacking behind, and 2) opportunities to intervene are limited. Currently information is often only processed after more than a year on average. The dVi information over, for example, 2012 is provided by the 1<sup>st</sup> of July 2013. It is only judged upon by the 1<sup>st</sup> of November 2013. This creates a time window of, at maximum, nearly 2 years for corporations to engage in risk without formal regulators knowing. Minimizing this period can help in preventing much of the negative consequences.

Limiting this slack is hard. Brousseau and Glachant (2011) mention the potential use of what they call 'reflexive governance platforms' in regulating (physical) networks. Main notion is that in situations where success is dependent on multiple actors, regulators can engage with these actors in order to achieve compliance and success. In this case, engaging with the regulator potentially has positive effects for the individual actors. To some extent, this is also applicable for the corporation sector. Peers generally have notions on the performance of one another, thereby potentially able to prioritize work of regulators to limit the slack.

Corporations have few insight in each other, even though relatively much information is publically accessible. Regulators might participate in regional sector discussions where they present their analysis of the corporation performances in the region, but also over the region to national comparison. In combination with theme discussions (e.g. on risk management or geographic developments), or discussion on alternatives to improve, of regional best practices, both regulators as peers may learn from each other. This way, the discussion will switch from 'past' to 'present'. It

provides positive elements to peers as they may learn of each other (it is important the discussion doesn't go to 'naming and shaming'). It is likely mostly the 'best practices' will stand out. However, to both regulators and peers this indirectly makes clear the 'bad practices'. Other than regional sector meetings, this may also be done by, for example, participation on Aedes activities.

#### 9.4.4. Utilize interdependencies between peers

In section 9.3, it was argued to increase the interdependencies between peers to get a better information position. However, this also proved to be a barrier. Still, increasing interdependencies is not bad per definition. Many interdependencies between peers may provide an incentive to monitor each other more closely and interfere to each other earlier. However, it troubles interference when stakes are high. Peers only being dependent through the financial security structures makes it easier for peers to interfere on one another when stakes are high. Then again, this potentially limits the information position of peers and requires a formal position to interfere.

From this, it follows there is no optimum. One of two extremes is to be chosen. Which one is favorable heavily depends on other improvements in the functioning of peer monitoring. In the current situation, an increase in interdependencies is favorable from a peer monitoring perspective. This way, peers collect information they may share to regulators whom may then intervene.

### 9.5 Reduce context barriers on the ability of peers

From the analysis, three barriers in the context of the peer arrangement are identified that limit the ability of peer to monitor one another: the distance between peers, the not recognized formal indirect means and the dependencies on indirect and informal means (table 9.5). Each element is discussed below.

Table 9.5: Alternatives to reduce context barriers on the ability of peers

No.	Alternative
1	Align the security structure to the relations peers have
2	Give peers a formal role in regulator procedures
3	Strengthen relations between corporations and supervisors

#### 9.5.1 Align the security structure to the relations peers have

The security structures operate on a national level, i.e. over all 389 peers. However, peers only have some insight in a small number of these peers. Mostly, this is regionally oriented. Only for the bigger corporations, size seems to be an important indicator. This makes clear that there is a discrepancy between the scales in which the peer monitoring arrangement functions and the scale of the security structures. Alignment of these scales allows peers to better monitor one another. As, due to the other barriers, it is impossible for a corporation to monitor all its peers, this paragraph focusses on adapting the scale of the security structures. This paragraph argues using self-formed groups of corporations lightens both the task of peers and regulators to monitor individual corporations.

It is hard to define performance indicators and corresponding norms for corporations in general due to the complexity of corporations themselves and the environment they operate in. These are, amongst others, dependent on the size of the corporation, the demographics of the region the corporations operates and the activity of a corporation. Therefore, the CFV dashboard allows DAs to modify the norms for corporation.

By letting corporations categorize themselves, a number of advantages are achieved. Regulators are capable to categorize corporations on size and geographic location etc., but many relevant aspects (e.g. risk preference) are harder to grasp. Risk avoiding corporation won't allow (and risk) risk taking corporations in their group. Corporations avoiding (types of) derivatives won't allow corporations with active treasury policies in there group and so on.

The self-forming of groups makes it easier for regulators to set norms for corporations. Also, it may motivate peer in a group to define some group rule (including the setting of norms). If the latter is achieved, it forms a good basis for peer monitoring on the other regulator activities as well.

### **9.5.2 Give peers a formal role in regulator procedures**

Currently, corporations don't recognize means they may utilize to discipline a peer indirectly. It must be noted, there are not many them may utilize. This limits the ability for peers to regulate one another. On the other hand, peers are better able to give knowledge to information (confidential sources) Therefore, it is wise to give peers a formal role in regulatory procedures. By making the awareness of peers a full field in corporation judgment procedures, CFV can force corporations to gather data on peers and form an opinion on the data. Core condition is obviously that peer group sizes are limited which can be done in the above mentioned ways. A downside is this alternative allows from strategic behavior and regulatory capture.

By transposing the current CiP reports in 'group performance reports' a contribution of regulators to the functioning of this arrangement is made. This would make the regulator to corporation relationship focus more on the giving knowledge to information than on the collection of data. Less drastic, this can be implemented as a standard topic of conversation in a corporation visit instead of a full regulation field. Downside of the alternative is that corporation might consider it as a checkbox more than a contribution to regulation, resulting in the alternative just being a contribution to bureaucracy.

### **9.5.3 Strengthen relations between corporations and supervisors**

The dependency of corporations on regulators to intervene also hampers the ability of peers to monitor one another. The easiest way to reduce these barriers is to install interventions peers can make themselves. This results in a very similar discussion as in paragraph 9.3.1. For this reason, this (relevant) option is not further discussed here. This also holds for the alternative presented in the previous paragraph.

The alternative elaborated on here is to strengthen the relation between corporations and supervisors. In the current peer monitoring arrangements the relations between the corporation and the supervisor are very important. The stronger this relation is, the more corporations may benefit from the supervisor and vice versa. In strong relationships, peers are better able to utilize means available to regulators. In section 12.2, current developments in this relations are further discussed. A downside of a strong relation is the risk of regulatory capture.

## 9.6 Considerations on the most promising alternatives

This chapter identifies multiple alternatives to increase the functioning of peer monitoring in the Dutch social housing sector. This section briefly concludes on the most promising alternatives identified. In general, the hybridity of the Dutch social housing sectors provides many freedoms to engage in corporation risk taking. Corporations are independent from the government, reducing the ability of the government. On the other hand, corporations are protected from the market thereby limiting the incentives for the effective and efficient allocation of resources. Transitioning the sector to a full market will provide the most incentives to limit moral hazard and take risk efficiently, but will hamper the role of peer monitoring.

Applying peer monitoring in smaller groups increases the ability of peers to monitor one another. Though the willingness is already increasing due to current sector development, risk sharing over the same group will further increase the willingness. The groups are best formed by corporations themselves as this will automatically sort corporations on the information they have of one another and their risk preference. Hence, the grouping of corporations also contributes to the prioritization of corporations for regulators. Other alternatives that increase the willingness of peers to monitor one another often introduce the paradox that higher incentives increase the willingness of peers to monitor, but also increase moral hazard in the peer relationship.

The existence of regulators limits the willingness of peers to monitor one another. But now willingness is increasing, peers prove dependent on regulators to discipline one another. The other way around, peers may contribute to regulators in the signalling of corporation risk taking. This makes closer cooperation between regulators and corporations a promising alternative for the ability of peers to monitor one another better.

## 10. Other alternatives on the management of moral hazard

The core focus in this research is the potential of peer monitoring in managing moral hazard. As such, this study identifies a number of barriers limiting the functioning of peer monitoring. Chapter 9 presented alternatives to reduce these barriers. However, two main issues limit the effectiveness of the alternatives. First, stronger incentives for peers to monitor one another generally also imply higher incentives for moral hazard. Second, regulatory arrangement generally have a focus to look at the past, while key in managing moral hazard is to prevent risk from being taken.

This chapter therefore focusses on the management of moral hazard more than on the functioning of peer monitoring. In studying moral hazard, corporations proved to experience many freedoms in their risk taking. Three elements in particular contribute to this:

- Opportunities provided by legislation
- Financial security structures
- Financing through volumes of facilitation

Alternatives on all three elements are presented in the subsequent sections of this chapter. This elements are strengthened by the hybrid sector structure, placing corporations between governments and markets. Alternatives to this hybridity are discussed in the fourth paragraph. The fifth and final section presents an alternative that discusses the preferred size of corporations in terms of risk.

### 10.1 Limit opportunities provided by legislation

From a legal perspective, corporations currently have many freedoms to engage in risky activities. Especially the allowance to invest in the ‘liveability’ of neighbourhoods and the surrounding of the neighbourhood is a poorly demarcated field that is used as argument for a wide variety of projects. Therefore, many organizations, including corporations themselves, currently desire stricter legislation.

The call for stricter legislation is one traditionally made when crises occur. In the Dutch social housing sector, stricter but especially clearer legislation may be helpful. Corporations are currently allowed to engage in a wide variety of commercial activities. These commercial activities don’t directly contribute to their core goal, but are allowed as the core objective of social housing is loss giving. However, in practice it turns out the returns on most commercial projects corporations engage in are low on return or even loss giving. Simultaneously, these variety of activities corporations may engage in hampers peers in their monitoring effort.

Considering the limited added value of commercial activities, an alternative to improve peer monitoring efforts is to limit the variety of activities a corporation may engage in. This significantly reduces the regulation complexity for both peers as well as regulators. A positive side effect is that it potentially also reduces risk taking behavior in the sector. In fact, these two reason also convinces some of the Aedes members (Aedes, 2013) to engage less in commercial projects. The second reason may be doubted, as corporations will continue to seek status. Hence, it may be expected that risk taking will just take place in some other fields. Still, it proves social housing projects are often less risky than commercial projects. One way or the other, stricter regulation does not hamper the strengths of the financial security structures. Hence, it is a positive alternative to manage moral hazard better.



## 10.2 Redesign the financial security structures

As the financial security structures provide the strengths of the moral hazard in the sector, they are at also the core of managing moral hazard. The strengths of this structure is directly related to the sharing of risk. This makes there are limited opportunities for a redesign in which the current strengths remain intact.

Currently, peers benefit from the security structure, but are also the first to pay for the negative consequences. While keeping the strengths intact, the negative consequences of the moral hazard in this relationship can only be displaced to other actors. In fact, this means the incentive for peers to monitor one another is displaced. Though this would further limit the potential of peer monitoring, it also provides the opportunities to align the monitoring incentive to those having formal abilities to monitor corporations. Note this alternative basically suggest to go back to the security structures as they were before the financial autonomization. Obviously, the opposite is also possible: give those with the incentive (currently peers) the formal means to be able to monitor one another. This option was already discussed in chapter 9.

## 10.3 Go back to financing based on actual projects

Corporations also gained leverage to take on risk by the working of WSW through facilitation volumes, i.e. guarantees for (a predetermined amount of) loans in the future apart from underlying factual projects. This makes corporation have easy access to big amounts of cheap financing. By returning to the old situation in which corporations have to request financing for each individual project, taking risk that is out of proportion is better monitored.

Main advantage of facilitation volumes is that corporations are then able to attract amounts of financing when it serves corporations best, often resulting in a small interest advantage as well. This advantage is lost by returning to the old situation. However, the advantage seems marginal. Hence, this alternative contributes to better managing moral hazard as it comes at relative low cost for the strengths related to the moral hazard.

## 10.4 Choose between governments and markets

Corporations operate in a hybrid sector, i.e. in between governments and markets. This basically means corporations are free to behave like market players, but miss some incentives on efficiency as they are also partly shielded from market forces. Corporations have to balance between their public goal and their competitiveness. This reduces incentives on risk taking efficiency. Hence, considering moral hazard, it is wise to formalize the dominant perspective for corporations: their public goal ('governments') or their competitiveness and market efficiencies ('markets'). This strengthens the incentives supporting the perspective.

This alternative was already discussed in paragraph 9.4.1 from the perspective of peer monitoring. Paragraph 9.4.1 is also applicable here. However, here focus is given more to the network context of the decision. Focus on the public goal brings corporations closer to governments and therefore also closer to controls of parliament. Focus on markets, might lead to efficiencies enforced by third parties. This research refers to these type of third parties as 'lighthouses'. Both extremes offer incentives to manage risk and moral hazard better. Whether the focus of a corporation should be on governments or markets is less relevant than the notion that through hybridity incentives are weakened.

## 10.5 Optimize the size of corporations

Typically, risk is often mathematically represented by probability \* impact (Saaty, 1987). This mathematical relation is generally considered uncorrelated. For individual projects, this might be true. For risk sharing over corporations, however, probability and impact are correlated.

Abstractly speaking, impact is closely related to the size of a corporation. For example: when a big corporation needs financial restructuring support, it will need more than a small corporation would. Simultaneously, a bigger corporation is also better capable to deal with losses internally than a small corporation. Hence, focussing on risk, the probability on using the security structures is lower for larger corporation (i.e. those with higher impacts). As an example, Servatius was able to deal with €200 million of losses on the Campus project internally. A corporation with 1000 housing units (with an approximate yearly turnover of €6 million), would not be capable to do so. Hence, there appears to be a negative correlation between probability and impact in the risk of security structures in the Dutch social housing sector being utilized.

This negative correlation may suggest an optimal corporation size being existent in relation to risk taking. The one extreme is represented by a few big ('system') corporations that have a high capacity to deal with risk internally (and, hence, a low probability to use the financial security structures). The other extreme is represented by many small corporations that relatively quickly need the security structures, but will ask for relatively limited contributions.

For managing moral hazard, it thus seems a few big 'system' corporations are favourable. This is correct for the risk materializing, i.e. the sharing of consequences, but not for the underlying behaviour. Social cost still occur in terms of loss in social capital. In the case of many small corporations, also 'smaller regular' risk may lead to claims on the financial security structures. As such, one might even argue small corporations would incentivize moral hazard as any risk is covered through the security structures. Also considering the management of moral hazard through a peer monitoring perspective suggests an optimum. Small corporations will provide more, but weak incentives. Big corporations will provide few, but strong incentives. For managing moral hazard, the optimum seems to lay more on the side of smaller corporations as this prevents the negative consequences of moral hazard, i.e. loss in social capital, the most while preserving the strengths of risk sharing.

## 11. Conclusion

The Dutch social housing sector is characterized by moral hazard. In this research moral hazard is defined as strategic behaviour of an actor, from which the positive effects of risk taking are for the actor itself, while negative effects are (partly) shared with others. Preconditions of moral hazard are information asymmetry, separation of ownership and hidden action. Scholarly literature suggests peers have less information asymmetry as compared to traditional 'vertical' regulators. This makes peer monitoring potentially more effective to manage moral hazard (i.e. limit negative consequences, while retaining the strengths). It is expected, peers are willing to monitor one another as they share in the negative consequences of each other's risk taking. This research studies the effectiveness of peer monitoring in managing moral hazard by answering the following question:

*What is the potential of peer monitoring to manage moral hazard between Dutch housing corporations and can this be improved?*

Peer monitoring may well have the potential to manage moral hazard better as compared to vertical regulators, but peers currently lack the ability and willingness to do so in the Dutch social housing sector. The design and sector context of the peer arrangements are decisive on the success of peer monitoring in this sector. Peer monitoring only starts to show potential through very subtle arrangements since the economic crisis and the collapse of Vestia. Improvements in both the peer arrangements and its context can professionalize the functioning of peer monitoring in managing moral hazard, but will often also increase the moral hazard itself. These conclusions are elaborated on below for the case of the Dutch social housing sector.

### *Four barriers in peer arrangements limit the success of peer monitoring*

Within the peer arrangements, four barriers are found to limit peers monitoring one another: 1) peers don't share information voluntarily, the existence of many peers makes peer monitoring 2) costly and 3) have a low risk for peers, and 4) peers have few means to intervene. This paragraph discusses these barriers and suggests improvements to reduce them.

Information is not shared voluntarily and peers have no means to gather information other than what is publically accessible. Also, the Dutch social housing sector comprises 389 corporations, all sharing their risks. This makes monitoring one another a very costly exercise. Formalizing the position of peers to gather information might help in this respect, but also other options are identified. For example, peers can better make use of information made available by regulators and third parties ('lighthouses').

Monitoring many peers also lowers the willingness of peers to monitor one another as risks are dispersed over many parties, i.e. the potential cost for peers are relatively low. The incentive will increase when the sharing of consequences is more specified to those best able to monitor the other. This is achieved by making corporations shareholders of each other's organizations or finance corporations in groups. All of these alternatives, however, also increase the moral hazard itself.

Fourth, corporations lack formal means to intervene at one another when they deem this necessary. This is resolved by making corporations shareholder of each other's organizations. Another alternative is through formalization through legislation, regulators or peer organizations like Aedes. This latter alternative will, however, most likely still require some form of centralization.

### *Context barriers to monitor one another*

On top of the above mentioned barriers, the sector specific context of the Dutch social housing sector, imposes additional barriers to the functioning of peer monitoring: 1) there are many freedoms to engage in risk; 2) though peers have multiple interdependencies, they are competitive and consider each other as autonomous organizations; 3) a lack of precedents exists along with formal regulators. This paragraph discusses these barriers and improvements to reduce them.

The willingness of peers to monitor one another is reduced by the many freedoms offered by legislation and the hybrid sector characteristics corporations operate in. The hybridity of the sector makes corporations fall in between governments and markets, thereby being less sensitive to incentives from both. These freedoms can be limited by stricter legislation (a claim also made by the sector itself) and positioning corporations either as government instances or full market players. A third option would be to stop the financial security structures, but this significantly affects positive elements of moral hazard and is therefore not appreciated.

Risk sharing is not the only relation between peers; amongst others they have a competitive relationship to each other. The interdependencies makes peers generally willing to gather information on each other but less willing to intervene at one another, although since the Vestia case the attitude towards information sharing improves. Reduction of the interdependencies will increase the willingness to interfere at one another but reduce the willingness to gather information of one another. However, it is this latter aspect that most contributes to the supposed strength of peer monitoring: reducing information asymmetry.

A lack of precedents and the existence of regulators also lower the willingness of corporations to monitor one another. This slightly changed since the 'Vestia precedent' resulting in €700 million loss to be covered by peers. The security structure can be redesigned to cope with more claims, but this also increases the moral hazard. Formal regulators as centralized organization turn out to be necessary to discipline peers. Still, currently peers have no access to regulator tools, thus implying the importance of the role of peers in formal regulation.

### *Contribution of findings to the general potential of peer monitoring in managing moral hazard*

Though this research only studied the Dutch social housing sector, the identified barriers have implications for the potential of peer monitoring in managing moral hazard in general. First, the sharing of risk provides a strong incentive to monitor one another when risk materialize, but is just one of the incentives that occur. Other incentives may weaken the risk sharing incentive. Hence, also the incentives in the context of the peer monitoring arrangement are relevant for the functioning of peer monitoring. Paradoxically, it is found that strengthening the incentive to monitor one another in most cases also strengthens the moral hazard in the peer relation.

Second, the incentives to monitor one another should be aligned to the system that provides the ability to monitor one another. This holds for peers, but also for others supposed to regulate. If willingness and ability are not aligned, good cooperation is necessary to align the best possible.

Peer monitoring is argued to have potential through the reduction of information asymmetry, especially in giving availability to information. However, this is irrelevant when peers do not have the ability to gather information.

## 12. Recommendations for further research

This research studies the potential of peer monitoring on managing moral hazard in the Dutch social housing sector. Though the findings of this research are already relevant for the sector and interesting for science, they are also bound to some limitations that imply grounds for further research.

### *Recommendation 1: Study more corporations to improve the generalizability of results*

First, and most obvious, this research only studies the practice of three of the 389 corporations in The Netherlands. In the selection of the three corporations studied, much attention was given to the representativeness of the corporations selected in the 'population' of corporations. However, giving the variety of dimensions corporations can be differentiated on, i.e. size, region, demographic developments, risk profile, competitiveness of environment, activity of municipality, urban/rural location etc., more cases have to be studied to be able to generalize the findings to the sector.

### *Recommendation 2: Study peer monitoring arrangements in other sectors to improve the generalizability of results into theory*

Results of this study oppose to established scientific literature significantly. To study the generalizability of the results of this study to the level of more general scientific literature on the effectiveness of peer discipline, it is relevant to study peer monitoring arrangements also in other sectors than the Dutch social housing sector. In the Netherlands, an example is the Banking sector, in Europe an example is the European Union, outside Europe, an example is the Australian federal states.

### *Recommendation 3: Study the effectiveness of peer monitoring on managing moral hazard on multiple levels*

Peer monitoring can take place on multiple levels. In the examples named before recommendation two, already a differentiation can be made between sectors and unions. Peer monitoring, as well as moral hazard, may also take place in smaller settings like students groups writing reports. Scale, being a rough indicator for complexity, may also influence the effectiveness of peer monitoring for managing moral hazard.

### *Recommendation 4: Study the effect of forming of groups on the effectiveness of peer monitoring*

### *Recommendation 5: Study the effect of group size on the effectiveness of peer monitoring*

The starting point of this research, peer monitoring being an effective arrangement for managing moral hazard, is for a significant part based on findings of Stiglitz at the Grameen Bank of Bangladesh (chapter 3). Two factors successful in the Stiglitz study are also argued to be successful in the Dutch social housing sector: small peer groups and self-formed peer groups. The effect of scale and the forming of groups appear relevant and can relatively easy be researched through experiments. This study contributes to identifying balances in which peer monitoring functions best.

*Recommendation 6: Study the effectiveness of the proposed alternatives*

*Recommendation 7: Study the applicability of the proposed alternatives*

*Recommendation 8: Study the cost of the proposed alternatives*

*Recommendation 9: Study the opposition to the proposed alternatives*

The alternative identified to improve the functioning of peer monitoring in managing moral hazard are only roughly shaped ideas that require further research on their effectiveness, applicability, cost and opposition before being implemented.

*Recommendation 10: Study the alternatives to limit moral hazard apart from peer monitoring*

In designing alternatives, the focus of this research is on improving the effectiveness of peer monitoring in the Dutch social housing sector. However, there are also opportunities to reduce moral hazard in the sector. Moral hazard exists through the financial security structures to prevent corporations from bankruptcy. Limiting, or even removing, the financial security structures, limits the moral hazard in its very core.

The ten recommendations identified above are non-exhaustive. Many more items for further research can be thought of. However, this list seems promising for both help improving the management of moral hazard in the Dutch social housing sector as well as deepening the knowledge on the functioning and effectiveness of peer monitoring (in managing moral hazard) in more general terms.





A glass sphere, likely a Christmas tree ornament, is shown in a close-up shot. The sphere's surface is highly reflective, mirroring the surrounding environment. The reflection clearly shows a two-story house with a gabled roof and several windows, surrounded by the bare branches of trees against a bright sky. The sphere is set against a blurred background of green foliage, which also appears as a soft, out-of-focus reflection on the sphere's surface. A semi-transparent red rectangular box is centered over the middle of the sphere, containing the word "Reflection" in a white, sans-serif font.

Reflection

## **13. Reflection on current developments in the sector**

In discussing the current developments in the Dutch social housing sector, I distinguish two fields. First, developments on sector structure (under the responsibility of BZK) are reflected upon. Second, the potential effects of current internal reorganization of CFV concerning peer monitoring is discussed.

### **13.1 Developments on the organization of the Dutch social housing sector**

Ever since the autonomization of corporations, the Dutch social housing sector has been topic of fierce political discussion. Often, these discussions took place in the context of the entire governmental housing policy. Many reports were written by the Aedes lobby, but also on behalf of the ministry responsible for housing (first VROM, followed by BZK). Other than reports published under the responsibility of the minister these include, amongst others reports of the Hoekstra committee, Schilder committee and De Boer committee (Hoekstra, Hoogduin, & Schaar, 2012). However, over the years, not much changed until 2011.

#### **13.1.1 Herzieningswet**

In May 2011, the so-called ‘Herzieningswet’ was submitted to Dutch parliament. After some changes, it was approved by the House of Representatives in July 2012. Objective of the Herzieningswet is to improve the functioning of corporations in their social goal. Therefore, extra attention is given to the relation (formalized through performance contracts) between corporations and the municipalities they operate in. Also, CFV is transposed in the Financial Authority on corporations (FAw, Dutch: ‘Financiële Autoriteit woningcorporaties’). In this transition, CFV also gains means to intervene on and sanction corporations (Eerste Kamer, 2013).

Both developments may contribute to the functioning of peer monitoring in the sector indirectly. In this thesis, it was shown the performance contracts between corporations and municipalities provide the basis for platforms in which corporation discuss business. Also, the performance contracts provide ground for municipalities to intervene on corporations, whether or not based on peer findings. The strength of performance contracts lies in its provision in regional regulation, i.e. on similar scale to the operational field of most corporations.

CFV currently has no means for intervention, other than safeguarding its information (Hoekstra, Hoogduin, & Schaar, 2012). Within these limits, CFV can still intervene quite significantly. For example, letting a corporation provide information on each activity before it can engage (with consent of CFV on solvability and continuity) in that activity (CFV, 2013a). However, not having formal ‘sticks’ to intervene sometimes proved hard in practice (König, 2013; Verbraeken, 2013a). Adding sticks to the arsenal may prove helpful in managing moral hazard in general and the functioning of peer monitoring in specific. CFV is the formal sector regulator closest to corporations. As such, it is best aware of the corporation playing field, including the behavior and risks taken by individual corporations. Hence, the Herzieningswet brings intervention ‘closer’ to the sector in specific for the functioning of peer monitoring by helping corporations over the burden that CFV is the way to go to report issues of peers and is able to act upon these notions.

### 13.1.2 Adaption on the Herzieningswet in 2013

Approved by the House of Representatives in July 2012, the Herzieningswet is still to be approved by Senate. In between, multiple changes have been made to the proposition. One, however, is of particular interest: incorporation of CFV under BZK.

In the latest report on regulation in the Dutch social housing sector, a committee chaired by Rein-Jan Hoekstra, argues for an organizational distinction between the regular supervision on a corporation, intensified supervision on a corporation and the financial restructuring of a corporation (Hoekstra, Hoogduin, & Schaar, 2012). Although this distinction is currently introduced in the CFV organization for its transition to FAW (see section 13.1.2), a parliamentary inquiry committee just started studying the sector regulation (CFV, 2013b) (again) and the Minister of the Interior develops a plan to bring back the CFV under the ministry (Verbraeken, 2013b).

Distancing CFV from ministries has been a choice made well aware (Scheltema, 1997). Respecting ministerial responsibility (Hoekstra, Hoogduin, & Schaar, 2012), distancing was a well-aware decision based on political accountability (Commissie Borghouts, 2000). Stef Blok, Minister of the Interior, argues bringing back CFV under the ministry adds to better information exchange and communication to WSW (Rijksoverheid, 2013).

Blok motivates his decisions on findings of the Hoekstra committee (Ministerie van Binnenlandse Zaken en Koninkrijksrelaties, 2013b). However, Hoekstra also indicates the financial supervision is to be independent from policy makers (Hoekstra, Hoogduin, & Schaar, 2012). It might prove true that information exchange between regulators is better when CFV is internalized to BZK. Corporation financial performance and housing performance is strongly interdependent and regulators on these fields are spread. However, financial supervision is a typical business that requires dedication (Schilder, Mosch, & Hage, 2006). It is for this very reason, financial regulators are often placed outside governments (Bogaarts, 2013). Some Dutch examples are DNB, AFM and NMa (now ACM).

For managing moral hazard, it is therefore questionable how effective internalization of CFV will be. Internalization almost surely increases the psychological distance between corporations and the financial regulator. Considering a core condition of moral hazard to be asymmetric information, keeping CFV outside the ministry therefore seems more logic. On contrast, this thesis argues that in the current situation, organizations closer to the risk taking corporation don't necessarily prove to function better. However, two things are different in this case. First, it is the core business of CFV to financially regulate corporations. Second, CFV has the means to secure information in contrast to peer corporations. Hence, distancing CFV further from corporations is a questionable policy to improve the management of moral hazard. It is speculated that this distancing might also hamper the relationship between CFV and corporations, thereby negatively influencing the potential for peer monitoring.

## 13.2 CFV reorganization

In preparation to the transition from CFV to FAw, CFV is already reorganizing internally. This paragraph reflects on this reorganization for the peer monitoring potential in managing moral hazard.

Previous, CFV supervision was organized by DAs assigned to regions. DAs regulated all corporations within their region. On average, DAs had about forty corporations each. These corporations may vary in size, activity pattern, risk preferences, financial performance etc. As a result, a DA could have a 'best of class' corporation and a corporation in financial restructuring and anything in between. In principle, there was no automatic refreshing of the corporation portfolio of a DA. As a result, some DAs had corporations in their portfolio over five, even up to ten years.

Hoekstra suggests this may not prove the way to go. He argues a clear distinction between the regular regulation, intensified regulation and financial restructuring. Including this recommendation in the transition to FAw, CFV now distinguishes between a department for the regular supervision and a department for the intensified supervision. In these departments, inspectors (as they are now called), work in teams. Furthermore, corporations are no longer categorized on region but on size (as a mix of number of vhe and total balance account), distinguishing between small, middle and large sized corporations.

From a regulatory perspective, these developments seem promising. Obviously, the risk of regulatory capture was relatively big. This was also proven in the WSG and Servatius case. Working in teams significantly reduces this risk. Furthermore, the new design is based on clear and distinct criteria. Corporations are now categorized more on what they are then on where they are.

Considering peer monitoring for managing moral hazard, the old situation had its advantages. Although sensitive for regulatory capture, DAs build up a relative strong relationship with board of corporations. As corporation executives often have contract for an undefined period of time (and, in practice, work at corporations for longer times) these relationships may be valuable for the peer monitoring potential. Potentially the capture risk might work vice versa, i.e. the corporation being captured by the DA for making peer monitoring work more effectively.

Working in teams not necessarily breaks these relationships. However, it shows the importance of single contact persons (backed by team members). Also, in this respect, corporation pools for inspectors should not replenish too fast. No longer working in the regional context also may hamper peer monitoring as corporations prove to monitor their geographic peers most closely. This makes distinction between supervision and financial restructuring still valid, as they concern a completely different approach. This peer monitoring perspective is quite opposite to the regulatory perspective. No single answer is best in this discussion. However, it seems wise to proper balance between the two.

## **14. Reflection on this research**

This chapter reflects on the meaning of this master thesis research. Therefore, it first reconsiders the existence of moral hazard in the sector. Second, it discusses the added value of this these from both a scientific and a social perspective.

### **14.1 Studying moral hazard in the Dutch social housing sector**

Moral hazard, being an old term, is reinvented as topic of study in insurance in the late 1960s early 1970s. From there, the concept moved to more social sciences through economic theory. Still, moral hazard seems underexplored in the social sciences. Few research has been done on moral hazard occurring in practice, especially on an industry sector level. Undoubtedly, the unobservability characteristic of moral hazard proved to this.

Using horizontal regulation, what in this study is called peer monitoring, to mitigate moral hazard is even studied less. The idea of horizontal arrangements is named differently by various authors. In horizontal regulatory arrangements, one can distinguish between arrangements through peers or through market forces. The ambiguity in scholar literature concepts, shows the contemporary field of science this research was performed in.

The topic not being actively studied causes little is written on peer monitoring arrangements in managing moral hazard in general. Social housing (at least in the Dutch way) is no real international field of research. Though housing markets are studied in international scholarly literature, social housing is typically a Dutch field studied by scholars in spatial planning. This makes the specific literature on sector dynamics, sector risk taking and sector regulation fairly limited, thereby forcing to 'read between lines'. Also in non-scholar literature this was mainly the case due to the sensitivity of the subject.

As this thesis states various times, in 2010 for the first time a real claim was made on the peer financial security structures (the SGBB case). This was followed by Vestia in 2012, claiming €700 million from its peers. The Vestia case costs peers (tens of) millions of euros. The functioning of the sector regulation and the financial security structures is considered an open wound. To put it bluntly, the question of this research is 'peers, why didn't you do anything?'. The context above makes clear this is a very, very sensitive question. The sensitivity specifically influenced this research in studying WSG. In the WSG financial restructuring process, peers are to buy equity of WSG thereby damaging their own investment capacity. The selling of WSG equity being guided by CFV made WSG not participating in this research.

Another limitation on the content on of this research lies in the need to evaluate peer monitoring functioning with those who are able to see peers (and take risk themselves). Corporations are characterized by relatively small top management layers. Contact with peers is bound to executive level. Therefore, it was required to speak to the managing directors for this study. For a student, these are not the easiest people to approach. Amongst others, CFV greatly contributed to this respect. Hence, I am sincerely very grateful for this opportunity provided.



Final to this section, already hinted on, is the question whether moral hazard is or is not present in the sector. Sector experts argued financial security structures (and thus risk spreading over corporations) played a role. On the contrast, CFV inspectors argue implications of claims on the security structures are so big for both executive and supervisory board (these are mostly fully renewed), they don't believe risk spreading is an active consideration in risk taking. Although unsure on moral hazard taking place or not, the findings on peer monitoring still hold. Maybe, over some years or even decades, memoirs will provide clarity.

## **14.2 Studying regulation on moral hazard**

The focus of this research lies on the potential of peer monitoring to manage moral hazard, i.e. limit the negative elements while remaining the positive elements of risk sharing. This research treats peer monitoring as a potential regulatory arrangement for the management of moral hazard. However, in doing so, this research encounters some limitations. Most important notion is that moral hazard is not actively regulated upon. Hence, many regulatory arrangements are in place for other reasons. On the other hands, the moral hazard perspective may bring new light to these arrangements.

A good example is the current reform of CFV from regional DAs to teams of supervisors. This transition is for an important part inspired to reduce risks of regulatory capture. In the past, it proved that single DAs were assigned to a specific corporation for over ten years. Although this is a valid idea, the current transition to teams increases the burden of peers to inform CFV on other corporations. Hence, the transition damages. Obviously, a choice is to be made, but the current decision seems a little extreme. Though it is important to limit the risk of regulatory capture, the relationship of supervisors to corporations are relevant.

## **14.3 Relevance of this study**

In reflecting on the relevance of this study, there is distinguished between the scientific relevance (paragraph 14.1) and the societal relevance (paragraph 14.2) of this thesis.

### **14.3.1 Scientific relevance**

Peer monitoring is an understudied concept. Few authors mention the ability of it (naming it different ways). Those studying peer monitoring concepts seem to mainly focus on its positive effects and capabilities. The added value of this thesis lies in demonstrating that not always peer monitoring has positive effects. This research thereby specifically focused on the limitations on peer monitoring as an arrangement. The added value of this thesis from a scientific perspective main lies in the recognition of the importance of the context in which peer monitoring is expected for the effectiveness of peer monitoring. Although having its shortcomings, likely every study has, this thesis provides solid ground for further studying the conditions in which peer monitoring may prove successful.

### **14.3.2 Social relevance**

For decades, there has been discussion on the reforms of the Dutch housing market. Social housing being an integral part of this, also Dutch social housing has been topic of much discussion. Over the year, numerous reports have been written on how to adept the sector and its corresponding regulation. Some of the contemporary developments were discussed in section 14.1. This thesis forms an addition to these numerous reports available.

However, in discussing the sector and its regulation, the approach of this thesis is totally different. Ever since the Dutch law on housing was introduced in 1901, state aid was present in developing social housing and (governmental) insurances were in place for the financial restructuring of corporations. Since the autonomization, state aid and insurance remained present (though on the background) and now had to be paid for by corporations themselves. In contemporary discussions on the sector structure, very rarely attention is given to risk taking of corporations and the role of this (peer) insurance in this risk taking.

This thesis is directly focusing on this risk taking and corresponding insurances. In doing so, it discovers ideas on the reorganization of the sector not seriously argued before. It is expected that peer insurance might play a bigger role in disciplining the individual organizations in the sector. Vice versa, it might also be true that without the (peer) insurance, the risk awareness of individual organizations in the sector improves. Hence, even though findings are to be studied further, this report contributes to the discussion on the reform of the social housing sector by providing a different perspective in approaching the contemporary challenges.

#### **14.4 Further limitations of this study**

In the recommendations, many limitations of this research have already been identified. These limitations provide the basis for further research to be performed. This section reflects on the generalizability of findings. Second, there is elaborated on the core issue on 'managing moral hazard' and a limitation this imposes for this research.

##### **14.4.1 Generalizability of cases**

Corporations are very diverse organizations. Other than on size and geographic location, they are classified by their risk preference, activity specialization, engagement in commercial activities, activity in financing markets, legal form, demographic developments etc. This makes corporations hard to compare and limits the generalizability of findings. It is for this reason, much attention was given to the case selection.

For the generalizability, it is always better when more corporations are studied. However, what was striking was the alignment between the cases, even though each corporation was significantly different. Though surprising, this still doesn't improve the generalizability too much. However, in most interviews also other situations were discussed. These specifically concerned the deviations of the findings.

In an interview, the example was mentioned of a regional gathering in northern Friesland who made benchmarks. This brought corporations in a fight, making some withdraw their participation in the gathering. So, even the exception supports other main findings of this report. Another example is a corporation near Eindhoven reading the yearly report of a peer. Considering both district advisors are responsible for 40 to 50 corporations each, work in the sector for multiple years; these are the only examples they can think of, the generalizability of this research seems to slightly exceed the three cases studied.



#### **14.4.2 Managing moral hazard: move, resolve or deal smart?**

Managing moral hazard was defined as mitigating with its weakness while retaining its strengths. From the perspective of peers, the solution would be rather simple: maintain the security functions, but don't make peers accountable. Others accountable could be municipalities, the national governments, tenants etc.

The two main strength of the current moral hazard to be preserved is that of the cheap financing of corporations and the financing of projects largely through loan capital. This financing reduces the rents for tenants up to €35 per housing unit and enable corporations to engage in more activities. Hence, resolving the risk, for example by making corporations full market organizations, does not respect this strength. Moving the risk does not respect the theoretic potential of peer monitoring.

So, the focus of this research lies in 'preserving' the moral hazard at peers, but limiting the negative consequences for the peers themselves. As such, this research basically focusses on preventing the materializing of risk at a corporation on a level the individual corporation is hampered in its activities. As such, this research is not focused directly on moral hazard in the sector and the best ways to mitigate moral hazard. The core focus of this research lies in the potential of peer monitoring in regulating moral hazard under the current sector characteristics.



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## Appendices



## Appendix I – List of abbreviations

AFWC	Amsterdam federation of corporations ( <i>Dutch: ‘Amsterdamse Federatie van Woning Corporaties’</i> )
BBSH	governmental decree on the management of the social rental sector ( <i>Dutch: Algemene Maatregel van Bestuur Besluit Beheer Sociale Huursector</i> )
BCFV	governmental decree on the central housing fund ( <i>Dutch: ‘Algemene Maatregel van Bestuur Besluit Centraal Fonds voor de Volkshuisvesting’</i> )
BMV	Preservation of social capital ( <i>Dutch: ‘Behoud Maatschappelijk Vermogen’</i> )
BZK	Dutch Ministry for the Interior and Kingdom Relations ( <i>Dutch: ‘Ministerie van Binnenlandse Zaken’</i> )
CFV	Central housing fund ( <i>Dutch: ‘Centraal Fonds voor de Volkshuisvesting’</i> )
cip	sector report ‘corporations in perspective’ ( <i>Dutch: ‘corporatie in perspectief’</i> )
DA	district advisor
DAEB	Service for the general economic interests ( <i>Dutch: ‘Dienst Algemeen Economisch Belang’</i> )
DG housing	Directorate General of housing, building and integration ( <i>Dutch: ‘Directoraat-generaal Wonen, Bouwen en Integratie’</i> )
dPi	prospective information ( <i>Dutch: ‘de Prospectieve informatie’</i> )
DSCR	Debt Service Coverage Ratio
dVi	accountability information ( <i>Dutch: ‘de Verantwoordings informatie’</i> )
ICR	Interest Coverage Ratio
LTV	Loan to Value ratio
MVA	tangible fixed assets ( <i>Dutch: ‘Materiele Vaste Activa’</i> )
RWC	return value adjustment ( <i>Dutch: ‘Rentabiliteitswaardecorrectie’</i> )
SP	Warning points ( <i>Dutch: ‘signaleringspunten’</i> )
stiko	founding expenses ( <i>Dutch: ‘stichtingskosten’</i> )
SVWN	Foundation for the visitation of housing corporations in the Netherlands ( <i>Dutch: ‘Stichting Visitatie Woningcorporatie Nederland’</i> )
TI	Used as synonym to corporation ( <i>Dutch: ‘Toegelaten Instelling’</i> )
vhe	housing units ( <i>Dutch: ‘verhuureenheden’</i> )
VHV	social housing equity ( <i>Dutch: ‘Volkshuisvestelijk vermogen’</i> )
VOV	Conditional sales ( <i>Dutch: ‘Verkoop onder Voorwaarden’</i> )
Vpb	corporation tax ( <i>Dutch: ‘Vennootschapsbelasting’</i> )
VROM	Dutch Ministry of Housing, Spatial Planning and the Environment ( <i>Dutch: ‘Ministerie van Volkshuisvesting, Ruimtelijke Ordening en Milieu’</i> )
VTW	Association for supervisors of housing corporations ( <i>Dutch: ‘Vereniging voor Toezichthouders Woningcorporaties’</i> )



## Appendix II –New institutional economics

Neoclassical economics originated in the 19th century as a value and distribution theory (Colander, 2000). Over time, economist linked the terms of 'utility' and 'marginalism' (Swedberg, 1990). As a result, there is no full agreement on what neoclassical economics precisely contains as the term is widely used in various domains. However, in general, neoclassical economics is based on three core assumptions. The first is that actors act rationally over their set of choices. They do this based on full information, i.e. the second core assumption. Third, actors maximize their own gains in their decision making (Weintraub, 2002).

These assumptions do not come without critique. In neoclassical economics, the standard idea used in the context of risk treatment is the general equilibrium theory of Arrow and Debreu (1954). It supposes that 'the states of nature, which occur with exogenous probabilities, are observable' (Arnott & Stiglitz, 1988). Apart from the idea that all exogenous probabilities are observable (i.e. agents are fully informed) seems non-realistic, this approach to risk does not take into account the importance of trust, i.e. the fact that not everybody has access (and is able to use, i.e. give knowledge to) all information available (Arnsperger & Varoufakis, 2006).

The critiques on neoclassical economics are bundled in a field referred to institutional economics that was especially active in the early 20<sup>th</sup> century (Hodgson, 1998). Important contributions in the field were made by Hamilton (1919) and Commons (1936). On basis of the progressive insights in agency theory, transaction cost theory and theory on property rights, an attempt was made to integrate institutional economics and neoclassical economics using the term 'new institutional economics' (Williamson, 1975). It is this contemporary field of research that this study is based upon, as it (tries to) combine(s) the 'best of both worlds'.

Critics of (new) institutional economics argue that the concept of 'institution' is too generic to use for a specific theory, resulting in confusion on the core of the theory and the exact meaning of terms (Hamilton, 1692). A very important consequence for this study is that there is no universally accepted set of definitions has been developed as to what exactly distinguishes institutions from organizations in (new) institutional economics. In this study, the principles and criteria as described by North (1990) are followed as many scholars seem to follow his demarcation. North considers institutions to be the 'rules of the game', meaning they concern both the formal rules as well as the informal social rules. Organizations are then groups of people together with their governance arrangements (i.e. institutions) to coordinate themselves, i.e. the players of the game so to say.

### **Appendix III – Prudential regulation for managing moral hazard**

As moral hazard is hard to observe, proposed mitigation strategies mainly focus on measures to limit the risk-taking of firms beforehand. This is known as prudential regulation. Prudential regulation provides the limits ('incentives') for agents to limit their risk taking and simultaneously provides the monitoring possibilities/framework for the regulator. Typically, prudential regulation consists of a mixture of entry restrictions, capital requirements and the monitoring of transactions (Hellmann, Murdock, & Stiglitz, 2000).

By entry restrictions, only a specific type and/or amount of organizations is capable of participating in a market. Entry restrictions are often imposed by governments to ensure the quality and safety of services (Hellmann, Murdock, & Stiglitz, 2000). Examples of entry restrictions imposed by governments for financial industries could be a specific legal status, statutory objectives, and minimal financial position. Entry restrictions are found in many industries, and are often arranged through licenses. Think of banks and pension funds (Rocha, Hinz, & Gutierrez, 2001), but also airlines (Oliveira & Huse, 2009), pharmaceuticals (Taggart, 1993) and social housing (Priemus, 2005). Though entry restrictions are commonly used, they may hamper competition within industries.

Capital requirements entail the assets that must be held by an organization compared to the money invested. It is through this requirements that governments try to limit the risk of default by ensuring that organizations will have enough capital to sustain their financial obligations (Barth, Caprio, & Levine, 2004). Although 'capital requirements' is a term mostly used in the context of banking (Hellmann, Murdock, & Stiglitz, 2000; Nier & Baumann, 2006; Krugman, 2009), similar principles apply in other industries including social housing. What it comes down to is ensuring an adequate position of organizations in terms of liquidity, solvability and (financial) continuity (CFV, 2012d). Or, to set a burden before others (i.e. peers in the case of Dutch social housing) are held accountable for the damage inflicted. Disadvantage of capital requirements is that they come at a cost as now assets cannot be used for investment (Hellmann, Murdock, & Stiglitz, 2000).

The third typical element of prudential regulation is the monitoring of individual transactions. In terms of agency theory, monitoring is used to check whether the agent (e.g. an organization) make his decisions in the best interest of the principal (e.g. government) (Holmstrom, 1979). An example of monitoring in the financial world could be to ensure there is sufficient collateral on a loan (Hellmann, Murdock, & Stiglitz, 2000). Holmström (1979) showed that if 1) the actions of an agent may have negative consequences for the principal, and 2) monitoring is costless, monitoring will result in gains to the principal. However, monitoring is not costless. In fact, it will likely bring quite significant cost. It will be very rarely that a principal is capable and willing to monitor each individual transaction (Sappington, 1991). Nevertheless, monitoring is considered a core element in the identification of issues in sectors, moral hazard potentially being one of them (Hellmann, Murdock, & Stiglitz, 2000).

## Appendix IV – Generalized letters for the approach of interviewees

In the search for interviews to serve as data source on the propositions, both corporations as CFV district advisors have been approached to participate in the research. This appendix consists of the letters send concerning the request of participation (in Dutch). The first section of this appendix presents the letter send to the CFV district advisors. The second section presents the letter send to corporations. In this appendix, both letters are included in generalized form.

### Letter to CFV district advisor

Beste [...DA...],

Zoals u wellicht weet schrijf ik op dit moment mijn afstudeerscriptie bij het CFV over (de omgang) met moral hazard in de corporatiesector. Als onderdeel daarvan bestudeer ik ook de gang van zaken rondom een aantal corporaties: Servatius, WSG en Eigen Haard. [...Een van deze corporaties...] is uw specialiteit en ik maak dan ook graag gebruik van uw kennis omtrent deze corporatie. Dit document zet de grote lijnen van mijn onderzoek uiteen, om zo uit te komen bij een aantal onderwerpen waarover ik graag een oordeel vorm door het bestuderen van de drie bovengenoemde corporaties. Ik concludeer dan ook met een concreet verzoek aan u.

#### Context van onderzoek

Zoals gezegd kijk ik in mijn onderzoek naar de omgang met moral hazard in de corporatiesector. Ik zal dit later verder specificeren, maar leg eerst graag uit wat ik versta onder moral hazard. Abstract gezien is moral hazard het idee dat het verplaatsen van risico een gevolg heeft op het risicogedrag van een corporatie. Toegepast betekent dit dat een corporatie meer/makkelijker risico aangaat omdat de positieve ‘uitbetaling’ van het risico voor de corporatie is, terwijl anderen de negatieve consequenties opvangen als risico’s verkeerd uitpakken. Eenvoudig gezegd gaat het om risico afwegingen van corporaties.

Wat de corporatiewereld bijzonder maakt, is dat financiële problemen ‘horizontaal’ (dus door medecorporaties) verdeeld worden, onder andere via het saneringsfonds en het WSW fonds en obligoverplichting. Dit concept is uniek en zie je verder vrijwel alleen (deels) terug bij en banken (Europese) landen. Puur theoretisch zouden corporaties dus ook een oogje op elkaar (kunnen) houden, gezien de financiële consequenties als zaken uit de hand lopen.

Tegelijkertijd zijn er toezichthouders, die in essentie het mandaat hebben vanuit zowel de politiek als corporaties zelf. Toezicht kent echter altijd zijn beperkingen. Enerzijds ligt dat aan puur praktische zaken als mankracht, het is onmogelijk iedere overweging van iedere transactie bij iedere corporatie te monitoren. Anderzijds zijn dat (politieke) keuzes op systeemniveau. Denk bijvoorbeeld aan de hybridestructuur, waarbij corporaties in principe vrij zijn te participeren in bepaalde commerciële activiteiten, waarbij er geen duidelijke restricties zijn op de omvang hiervan, waarbij typen toezicht zijn gesplitst, er misschien gebrek is aan interventiemogelijkheden etc.

In deze spanningen ligt dan ook de rol die corporaties potentieel kunnen spelen in het onderlinge (‘horizontale’) ‘toezicht’. Zij kunnen bijvoorbeeld toezichthouders helpen in de beeldvorming over collega corporaties en tekortkomende elementen in het toezicht duiden. Over de afgelopen jaren zijn er een aantal casussen geweest, waaronder Servatius en WSG, waarin (bijna) aanspraak is gemaakt

op saneringssteun en ook het ‘horizontale’ toezicht dus schijnbaar onvoldoende heeft gefunctioneerd. Mijn onderzoek houdt zich voornamelijk bezig met de volgende vraag: waarom?

### **Proposities van onderzoek**

Deze waarom vraag is natuurlijk nog erg breed. Ik hoop samen met u een beeld te krijgen van een aantal elementen die hierbinnen vallen. Ten eerste is het interessant te kijken naar de prikkels voor corporaties om medecorporaties (‘de burens’) al dan niet te controleren. Ten tweede is het interessant te kijken naar de hoeveelheid informatie die corporaties hebben of kunnen krijgen over hun burens. In andere woorden, weten ze voldoende van de activiteiten en financiële positie van de burens om zich redelijkerwijs een oordeel te kunnen vormen? Ten derde is de vraag welke middelen corporaties effectief tot hun beschikking hebben. Er zijn mogelijkheden om direct ‘de buurman’ aan te spreken, AEDES te benaderen of het CFV/WSW aan te spreken. Welke hiervan worden eventueel toegepast? Hierbinnen valt ook de vraag hoe het ‘verticale toezicht’ (CFV/WSW/BZK) omgaat om met deze ‘horizontale signaleringen’? Uiteraard zijn er veel verschillende verklaringen mogelijk, de open opzet van deze vragen is echter bewust.

### **Verzoek aan u**

Graag heb ik met u een individueel gesprek waarin we bovenstaande vragen aan de orde kunnen laten komen en kunnen toespitsen rondom de gang van zaken bij [...*uw specifieke corporatie...*]. Vervolgens zou ik dan ook graag een gezamenlijk gesprek hebben met [...*andere DAs...*] (de districtadviseurs van de andere corporaties) om uitkomsten van de individuele gesprekken te kunnen vergelijken.

In de tussentijd is er idealiter ook een gesprek met de [...*betreffende corporatie...*] en één omliggende corporatie. Binnen de corporatie is het belangrijk iemand te spreken die invloed heeft op de risicoafwegingen van de corporatie en relaties onderhoudt met medecorporaties (of in ieder geval in staat is om). Hoewel dit in eerste instantie doet denken aan een bestuurder/financieel directeur, is dit voor het onderzoek niet strikt noodzakelijk. Het gesprek met de corporatie zal een neutralere insteek krijgen en dan vooral gaan over hoe de relaties met omliggende corporaties invloed hebben op het ondernemerschap dat bij een private organisatie past. De interne bedrijfsvoering en risicoafwegingen zijn in ieder geval niet de hoofdzaak van gesprek. Vraag aan u is of u contact met de betreffende corporaties kan opnemen met de vraag een dergelijk gesprek te organiseren, al dan niet in uw aanwezigheid. U krijgt hiervoor van mij een apart verzoek (gericht aan de corporatie) dat als ondersteuning hiervoor kan dienen.

## Letter to corporation

Beste [...corporatie...],

U bent benaderd door [...DA...] om mee te werken in een onderzoek naar invloeden van corporaties op elkaars ondernemerschap. In dit document wordt dit onderzoek en de context ervan verder toegelicht. Mochten er na het lezen van of naar aanleiding van dit document nog vragen zijn, nodig ik u van harte uit contact op te nemen voor een toelichting.

### Introductie van het onderzoek

Het onderzoek fungeert als mijn eindschrijving voor de studie Technische Bestuurskunde aan de TU Delft. Technische Bestuurskunde is een opleiding die zich onder andere concentreert op de omgang met kritieke ‘netwerk’ sectoren. Los van bijvoorbeeld de energie en transport sector, valt ook de corporatiesector hieronder gezien het belang van de sector in de Nederlandse maatschappij en de lange termijn investeringen die de sector kenmerken.

In grote lijnen kent de corporatiesector parallellen met de energie en transportsector. De afgelopen decennia zijn nutsbedrijven, openbaar vervoerbedrijven en corporaties steeds meer privaat georganiseerd terwijl ze nog steeds een belangrijke publieke taak vervullen. Er is echter ook een uniek verschil dat fascineert. Door de zekerheidsstructuren van het CFV en WSW en volkshuisvestelijke bijdragen bent u financieel verbonden met elkaar. De kern van het onderzoek focust zich op deze onderlinge relatie. Ik voer het onderzoek uit bij het CFV omdat zij mij in staat stellen in een beperkt tijdbestek een grondig overzicht van de sector te verkrijgen.

### Gespreksonderwerpen

De verzelfstandiging van corporaties vraagt om ondernemerschap. Met ondernemerschap zijn onlosmakelijk risico's verbonden. Door de onderlinge financiële relatie tussen corporaties hebben, in vergelijking met andere sectoren, corporaties een sterker belang zich een mening te vormen over hun medecorporaties. In hoofdlijnen is deze gedachte ook terug te vinden in het adviesrapport 'Toezicht met Bite' dat AEDES in 2012 uitbracht. Ons gesprek zal zich dan ook richten op de volgende hoofdvragen:

- Welke overwegingen maakt u bij het al dan niet volgen van de risicoafwegingen (bijvoorbeeld het aangaan van projecten, aankopen van grondposities, afsluiten van derivaten etc.) van medecorporaties?
- Waarop baseert u uw mening over medecorporaties?
- Wat ziet u als mogelijkheden (bijvoorbeeld verzoek om interventie vanuit CFV) om de risicoafwegingen van uw medecorporaties te beïnvloeden?
- Welke van deze mogelijkheden zet u in?
- Een deel van de (formele) mogelijkheden loopt via het CFV en/of WSW. Wat is uw mening over de omgang van deze partijen met de door u verstrekte informatie over medecorporaties?

Bij voorkeur stellen we deze onderwerpen tweezijdig ter sprake. Dat wil zeggen dat niet alleen de (overwegingen bij) signalen die u geeft interessant zijn, maar net zo goed uw omgang met binnenkomende signalen.

## Gesprekscondities

Vanzelfsprekend kom ik graag bij u langs om dit interview af te nemen. Ik doe dit graag zo snel mogelijk, bij voorkeur in de tweede helft van april of de eerste week van mei. Tot slot kan ik mij voorstellen dat u vragen hebt rondom de openbaarheid van dit onderzoek. In dit licht is het handig voor u om te weten dat er vertrouwelijkheidsafpraak is gemaakt tussen de TU Delft en het Centraal Fonds met een looptijd van 20 jaar. Dit heeft onder andere tot gevolg dat vertrouwelijke informatie niet zonder schriftelijke toestemming van het CFV wordt gedeeld of gepubliceerd. U medewerking aan dit onderzoek valt onder deze regeling.

De vertrouwelijke variant is nodig voor het beoordelen van de scriptie en moet ook beschikbaar zijn voor de visitatie van de opleiding. Ook komt er een publieke variant van het onderzoek. De publieke variant is nodig omdat dit de scriptie is voor een onderwijsinstelling, waarvan het resultaat in beginsel publiekelijk toegankelijk is. Het CFV geeft aan welke informatie vertrouwelijk is en hoe deze informatie kan worden verwerkt (bijvoorbeeld geanonimiseerd) in een publieke versie.

Mocht u nog vragen hebben van welke aard ook, aarzel dan alstublieft niet contact met mij op te nemen via onderstaande gegevens. Ik ontmoet u graag later deze maand en bedank u vast voor uw tijd.

Vriendelijke groet,



Cornelis Eikelboom

T: 06 12 74 66 78

E: [Cornelis.Eikelboom@cfv.nl](mailto:Cornelis.Eikelboom@cfv.nl)

## Appendix V – Interview questions

This appendix provides the prepared questions for during the interviews as well as a support form for checking issues that are brought up during the interviews. The questions are written as if they would be asked to a corporation (either subject of study or peer). Questions were reformulated but content wise similar for the interviews with other organizations than corporations. The questions are categorized to the propositions they may serve.

Note that these questions are just a preparation of the interview. As such, their importance lies more in the subjects that are to be covered during the interview than literally asking these question in these order. The questions are formulated in Dutch as the interviews were held in Dutch. The role of the support form was not leading during the interviews, but served as a more detailed check for the interviewer.

### Interview Questions

#### *Interview introductie*

- Eindschrijft voor masteropleiding aan TU Delft
- Onderdeel van een breder onderzoek (met meerdere studenten) naar de invloed van wederzijdse (financiële) afhankelijkheden op risicoafwegingen binnen instellingen
- Mijn focus ligt bij de Nederlandse woningbouwcorporaties
- Waarbij u een van de corporaties vertegenwoordigt die wij in meer detail bestuderen, en dan vooral uw contact met de omgeving

#### *Persoonsintroductie*

- Wat is uw huidige functie?
- Wat is uw geschiedenis in de corporatiewereld?

#### *1) Vragen rondom de beschikbare informatie van medecorporaties*

- Kunt u iets vertellen over de kennis die u in het algemeen heeft van medecorporaties?
- Op basis van welke informatie komt u aan die kennis?
- Is deze informatie over medecorporaties eenduidig en hoe gaat u hiermee om?
- Hoe ervaart u uw kennispositie over uw medecorporaties ten opzichte van andere partijen zoals de gemeente, toezichthouders en corporaties in andere werkgebieden?
- Kunt u duiden van welke groepen corporaties u de meeste kennis heeft?
- Ervaart u bij risico's van medecorporaties verschillen tussen uw risicoperceptie en die van de betreffende corporatie?

#### *2) Vragen rondom het gevoel om wederzijds iets van elkaar te vinden?*

- Kunt u iets vertellen over ondernemerschap bij woningcorporaties na de bruteringsoperatie en risico's die daar logischerwijs mee gepaard gaan?
- Voelt u de behoefte u actief een mening over medecorporaties te vormen?
- Hoe ervaart en ervaarde u financiële zekerheidsstructuur die deze sector kenmerkt?
- Ziet u een rol voor corporaties in het toezicht op medecorporaties?



- Ziet u hierin onderscheid tussen voor u 'bekende' en u 'onbekende' corporaties?

3) *Vragen rondom de acceptatie van wederzijdse oordeelsvorming*

- Indien u risico's bij medecorporaties identificeert, waarom zou u deze wel of niet kenbaar maken?
- Hoe verwacht u dat medecorporaties en de rest van uw omgeving reageert als u dit doet?
- Is er een verschil tussen corporaties waarbij u makkelijker dergelijke signalen zult afgeven?

4) *Vragen rondom de mogelijkheden om in te grijpen*

- Welke mogelijkheden ziet u om medecorporaties direct aan te spreken op hun gedrag?
- Welke maatregelen heeft u om een gedragsverandering van een medecorporatie af te dwingen of te beïnvloeden?
- Welke mogelijkheden ziet u om gedragsverandering van een medecorporatie indirect te bewerkstelligen?
- Hoe effectief zijn deze indirecte mogelijkheden?

5) *Vragen rondom de sturingsmogelijkheden in interventiemogelijkheden*

- Hoe uitgebreid vind u uw mogelijkheden om het risicogedrag van medecorporaties te beïnvloeden?
- Acht u uzelf in staat in een specifieke situatie het beste middel te selecteren en effectief te gebruiken?
- Vind u dat beschikbare maatregelen voldoende flexibel kunnen worden toegepast op een specifieke situatie?

## Interview support form

### Proposition 1: Peers have information about each other's behavior

*Notice distinction between having information and give knowledge to information*

- Monitoring of ambitions
- Monitoring of activities
  - Social housing activities
  - Non-DAEB activities
  - Exit strategies for activities
- Monitoring of financial performance
  
- Contradiction between sources of information, i.e. information is contested
  - E.g. executives that are celebrated by the community
- Role of type of information (formal, informal etc.)
  
- Corporation has overview of peers
- Corporation has (substantiated) opinion on peers
  
- Role of geographic factor (difference local/national)
- Role of size
- Role of type of organization (e.g. care housing, student housing etc.)
  
- Availability of information on peers in comparison to others
  
- Risk en risk taking (en dan feiten en percepties)
- E.g. A kijkt naar B, weet A dat B de perceptie heeft dat hij risico aan het nemen is

### Proposition 2: Peers have a sense of urgency to regulate one another

- Experiencing and aware of peer-to-peer
  - financiële zekerheidsstructuur
  
- Historic success → reluctance
- Effect of the slope (on system level)
  
- Belief that peers can contribute
  - Along with / next to formal regulators
  - Regulatory (CFV/WSW/BZK) sticks
  - Regulatory (CFV/WSW/BZK) functioning
  - Spreaded supervision
  - WSW facilitation volumes
  
- Relation to own risk taking
- Peer observation may bring opportunities (opposed to set of alarm), compliance is just one interpretation

- Sense of urgency sprouts from system structure
  - hybrid structure with unsustainable core
  - wideness of opportunities to engage in non-DAEB
  - unequal competition on non-DAEB
  - Many activities in itself non-illegal
  - Habit of rising real estate values
  - Financiële zekerheidsstructuur
- Spreading of risk
  - Role of geographic factor (difference local/national)
  - Role of size
  - Role of type (e.g. care housing, student housing etc)

**Proposition 3: Peers may interfere with each other's business**

*Notice distinction between giving signals and receiving signals*

- 'Culture'
  - Non-intervention
  - Non-receiving
  - Image
- Market conditions ('good if you break, bad if I pay')
- Network effects (reciprocity and multi issue)
- And again
  - Role of geographic factor (difference local/national)
  - Role of size
  - Role of type (e.g. care housing, student housing etc.)

**Proposition 4: Peers have formal & informal means to intervene**

- Corporation has a formal moment/mean in which it can approach the peer, being:
 

...
- Corporation has a formal moment/mean to approach 'indirect actors' as CFV/WSW/BZK/municipality
  - For example by contacting the DA
  - But also during more formal procedures as the continuity and solvability judgment

- What is the effect of these efforts? Are they hampered by
  - Variety of signals
  - Deviation from formal information
  - Multiple principals
  - Regulatory capture
  - Non-illegal activities
  - Insufficient support by (independent) facts
- Corporation has an informal moment/mean in which it can approach the peer
  - AEDES meetings
  - Joint Municipality meetings
  - Network meetings
  - Informal lunches/dinners/drinks
  - Effect of these informal but direct means is dependent on
    - Group pressure (multiple peers should execute pressure)
    - Internal organization of 'sanctioned' corporation
    - The availability of a 'stick'
    - Insufficient support by facts
- Corporation has informal moment/means to approach 'indirect actors'
  - What is the effectiveness of these informal and indirect means / naming shaming

**Proposition 5: Peers have enough degrees of freedom to adjust regulation to the situation at hand**

- Difference direct and indirect intervention

Corporation has a variety of measures to achieve compliance

Corporation is able to put into effect measures appropriately

Corporation measures are 'flexible' (i.e. can be bend to best fit)

## **Appendix VI – Informal institutional environment**

This appendix elaborates on the institutions in the informal context of financial risk taking of corporations. Therefore, a distinction is made between the culture from which corporations operate and the culture of financial regulatory regime.

### **Culture of corporations**

Before the financial autonomization, corporations acted as dedicated bodies for the provision of housing of municipalities. After the financial autonomization, corporations were no longer formally financially dependent of governments, though loans of corporations are, in the end, still guaranteed by governments. As corporations still (formally) have to serve the social housing interest of a municipality, many corporations still closely cooperate with a single or limited number of municipalities. In practice, it is often the corporation in cooperation with the municipality that shapes the social housing interest. This culture of commitment to municipalities expresses itself by the co-development of entire neighbourhoods, including non-housing facilities. The relation also holds vice-versa, municipalities often only work with a limited number of corporations (Schilder, Mosch, & Hage, 2006). This makes that there barely is any real competition.

On the other hand, corporations also experience market opportunities since the financial autonomization. Hence, many try to expand in both size as well as activities. The drive for expansion is further strengthened by strong equity positions (Schilder, Mosch, & Hage, 2006), and the idea that real estate value will remain to increase (Boelhouwer, 2000). Corporations are allowed to engage in a wider pallet that strict social housing activities as their core business has a negative business model, i.e. the business model rests on equity build in their 'public period'. This negative business model has also been an argument of corporations to engage in more commercial activities.

These two competing norms created a 'bandwidth' of corporation cultures. One might argue that a transition is occurring from the traditional public dedicated bodies to private market organizations serving a public goal. What is interesting is that, over the entire scale, financial wealth and growth generally is not the highest objective. In both cases the objective focuses on real estate. In the 'market culture', this means prestige is considered more in terms of pluriformity in activities and growth in real estate units (CPB, 2010; VTW, 2012).

### **Culture of the financial regulatory regime**

As downside of the financial autonomization, there were concerns that corporation would not use their equity enough for investments in social housing. Corporations are, by law, not allowed to use equity for profit allowances. In other words, all financial gain has to be reinvested. Corporations are only allowed to have buffers to guarantee their financial guarantee. However, former minister of BZK Johan Remkes limited the expanses of corporations though real estate values increased.

It is from this arrangement that a culture developed of supervision focussing on the excess of equity of corporations. In the period of 2008-2010, this focus manifested itself in a so-called C-judgement on continuity. The C judgment meant that a corporation was assumed capable to engage in more activities that in proposed in the dPi data request (Conijn, 2013). Obviously, CFV also maintained 'regular' supervision during this period, classifying 20 corporations as financially weak (CFV, 2010o). Nevertheless, this culture leads to the paradox of a financial regulator stimulating corporations to invest more (Hoekstra, Hoogduin, & Schaar, 2012).

Furthermore, Hoekstra classifies the culture as an 'administrative' regulatory regime. Financial supervision was insufficiently proactive and risk based (Hoekstra, Hoogduin, & Schaar, 2012). Although Hoekstra does not provide any arguments, the statement carries elements of truth.

Corporations supply their regulators with information at least two times a year. Once, in July, with information for a solvability judgment ('dVi') and once, in February, with information for a continuity judgment ('dPi'). The two judgements are not directly comparable and/or mutual influential. The solvability judgment is about whether a corporation is currently able to fulfil its financial obligations, while the continuity judgment is about whether proposed future activities will bring excessive risk to a corporation's future financial situation (CFV, 2008). So, when the solvability looked good, there is no direct reason to include the continuity judgment.

However, when the initial data given by corporations raises questions or concerns, i.e. SPs (see appendix I) are triggered, further research is performed which may include bringing together the solvability and continuity judgment. The contribution of this further research is hardly seen in the final judgment presented to a corporation, hence it looks relatively standardized/administrative (Hoekstra, Hoogduin, & Schaar, 2012). Currently, a process is on-going to integrate the two judgements better. It is based on this observation that the regulatory regime was considered relatively 'administrative'.

The dPi also brings forward a third aspect. CFV tends to see the dPi data as the planned activities of a corporation. Corporations tend to see dPi data as a maximum of activities they undertake and want to get approved. So, the goals of the dPi are different between corporations and CFV. Where corporation try to get a 'carte blanche', CFV tries to make a judgement on the financial continuity of a corporation for the future.

Concluding, with hindsight, some argue there has been too much an attitude of giving corporations the benefit of the doubt as they engage in publically useful activities. This would have shifted the perspective as it was given by the crude data. Quite naturally, this is changing as more corporation need financial restructuring support.

## Appendix VII – Formal institutional environment

In this section, the formal institutional environment is discussed. The regulation on housing is anchored in the Dutch constitution and the law on housing (Dutch: ‘Woningwet’). These are discussed in the first and second section respectively. The law on housing is elaborated upon in the governmental decree on the management of the social rental sector (referred to as BBSH), and the governmental decree on the central housing fund (referred to as BCFV), that are discussed in the third and fourth section respectively. Important in the activities corporations may undertake and how these may be financed is also the governmental decree ‘tijdelijke regeling diensten van algemeen economisch belang toegelaten instellingen volkshuisvesting’. This is referred to as DAEB regulation and discussed in the fifth section. The sixth and final section then elaborates on the hybrid sector structure.

### Constitution

In February 1983, the following text was added to article 22 of the Dutch constitution (Rijksoverheid, n.d.d.):

*‘Bevordering van voldoende woongelegenheden is voorwerp van zorg der overheid’.*

This passage implies that the government (i.e. the minister) is responsible for housing. This article illustrates that social housing was long considered as a public activity. The fact that the sector is now financially autonomous and non-public organizations effectuate the article, do not affect the responsibility of the minister (Hoekstra, Hoogduin, & Schaar, 2012).

### Law on housing (Dutch: ‘Woningwet’)

The first version of the Dutch law on housing was introduced in 1901. Main objectives of the law were to limit the living in unhealthy living condition and to stimulate the build of new and proper houses for the weaker of society (Stuurgroep Meijerink, 2008). The law was adapted numerous times. When referring to the law on housing, factually the ‘Wet van 29 Augustus 1991 tot herziening van de Woningwet’ is meant (Rijksoverheid, n.d.e.). Considering this study on moral hazards concerns the financial stability of the sector, articles 70 and 71 of the law on housing are of special interest.

#### *Article 70: Authorized bodies in the interest of housing*

Article 70 discusses the bodies entitled to work in social housing, i.e. the corporations. Corporations are authorized by royal decree and may also lose their status that way. A governmental decree (i.e. BBSH) further defines the activities that a corporation is to undertake. All corporations are supervised by the responsible minister, apart from the matters described in article 71 (article 71 describes the role of CFV). Furthermore, article 70 states that the minister has the power to oblige corporations to do, don’t do, or ask permission for specific actions. Finally, in extreme cases, article 70 allows the minister to put a corporations under its own regime and assign its own administrators to the body (by court approval) for a maximum of two years (Rijksoverheid, n.d.e.).

#### *Article 71: The Central Housing Fund (CFV)*

Article 71 acknowledges the existence of CFV and defines two purposes. Firstly, CFV might subsidize the a) restructuring of corporations when they don’t have the financial means themselves, and b) activities of corporations according to a governmental decree (i.e. BCFV). Secondly, CFV supervises the corporations, and may install sanctions on them, in the way described by BCFV. Each year, CFV

has to update its policy rules that give insight in how CFV will give substance to its responsibilities as determined in article 71 and the BCFV. Each year, a report on the effectiveness and efficiency of CFV activities is sent to the minister. Every four years, CFV has to send a report on its effectiveness and efficiency to the Dutch parliament. The financial resources of CFV are gained by a contribution of all corporations, the height of which is to be approved by the minister (Rijksoverheid, n.d.e.).

### **Governmental decree on the management of the social rental sector (BBSH)**

BBSH is the primary governmental decree that sets limits to the activities that can be undertaken by a corporation and interprets the law on housing (Rijksoverheid, n.d.c.). Overall, the BBSH is a directional decree, i.e. it does not provide strict guidelines (Hoekstra, Hoogduin, & Schaar, 2012). This paragraph discusses the core elements of the BBSH relevant to this research.

#### *Article 11: General operations of authorized bodies*

Based on the law on housing, corporations may only operate in for the purpose of social housing. In practice, this statement did not seem to demarcate activities clearly. Therefore, article 11 provides a limitative sum up of activities that are allowed under the term social housing. Corporations are allowed for:

- Building, acquisition, and demolition of housing and appurtenances
- Maintaining and provisioning of housing and appurtenances
- Maintaining and improving the direct adjacent area of housing and appurtenances
- Managing, allocating and renting of residential housing and appurtenances
- Selling of residential housing and appurtenances
- Provision of services for residents directly related to the habitation
- Work that contribute to the performance of the previous listed activities

This list of activities is seen as the core responsibilities of corporations. In reality, corporations perform a wider variety of activities, based on article 12.

#### *Article 12: Quality of housing*

Through article 12, the variety in activities a corporation may perform widens. On the basis of article 12, corporations may use their resources for a number of activities not listed in article 11, in order to support the goals of article 11. Specifically, article 12b allows corporations to perform activities in specialized housing (for the elderly, handicapped or those who are in need or care):

- Building and operating residential care facilities, associated shared areas and physical care infrastructure for projects of supervised housing and real estate for housing residents that need care, nursing or shelter.
- Contribution to the establishment of arrangements in the sense of housing, care and services, with the aim to stimulate independent living.
- Provide an intermediary role for residents in respect to care and services
- Work that contribute to the performance of the previous listed activities

Article 12b is, again, quite specific in terms of activities that may be performed by a corporation. However, article 12a significantly widens the activities that may be performed by a corporation:

- Building, acquisition, and demolition of non-housing buildings



- Maintaining and provisioning of facilities on non-housing buildings
- Maintaining and improving the environment outside the immediate vicinity of housing
- Renting of non-housing buildings
- Selling of non-housing buildings
- Carrying out other activities that benefit the quality of life in a district
- Work that contribute to the performance of the previous listed activities

The only restriction of this activity is that the foremost objective of the activity is to contribute to the quality of life of districts where the corporation is active. However, this restriction is poorly defined. Hence, this article significantly broadens the possible range of activities undertaken by corporations.

Over time, this article widened the opportunities of corporations to engage in non-DAEB activities. However, it also appeared that over the years the opportunities of this article were also further utilized. For example, the selling of houses (article 11) was allowed already quite some time. However, just in the recent six years the selling of houses was booming as a way to finance new complexes. A similar story holds for the activities described in this article.

#### *Articles 21 and 22: Finances*

The articles 21 and 22 prescribe that corporations shall use such a financial policy, that there existence is financially guaranteed. All resources that are in excess of this, including the profit, is to be used for housing purposes (i.e. article 11 and 12) exclusively. In other words, there always has to be a relation between government means (e.g. guaranteed loans) and the public tasks of a corporation. This however brings quite a tension as, in the case of social housing, the public task is negative for the corporation equity and therefore requires other activities to guarantee continuity.

#### *Articles 44 and 45: Withdrawal of the authorization*

In case the minister argues that a corporation inflicts or, on the short term, will inflict damage to the enforcement or cause of social housing to such an extent authorization is no longer in the interest of the sector, the minister might withdraw the authorization of the corporation. This decision is to be taken by royal decree and published in the Dutch Government Gazette. The withdrawal will only become effective when the period of appeal has expired, or the appeal is decided upon.

### **Governmental decree on the central housing fund (BCFV)**

BCFV sets the framework in which the CFV has to operate as well as the main objective for CFV. The BCFV is a directional decree, just like the BBSH. Hence, it does not provide strict guidelines on how CFV is to control corporations. This paragraph discusses the core elements of the BCFV (Rijksoverheid, n.d.b) relevant to this research.

#### *Articles 4 and 5: CFV supervision on corporations*

Each year, CFV sends a report to the minister on the financial status of each corporation. This report also contains a judgment of CFV on whether the financial status of each corporation allows the corporation to attract the needed financial resources. Also, CFV sends a report to the minister on the financial status of all corporations together, i.e. a sector report.

In order to make these reports, CFV is allowed to claim insight in the information corporations have. Each corporation will also send its annual financial balance and report that is approved by an accountant to CFV, guided by a statement of the board of the corporation.

#### *Articles 6,7 and 8: Policy rules of CFV*

CFV publishes policy rules in the Dutch Government Gazette, and redefines and republishes them yearly. Amongst others, the policy rules at least identifies the criteria CFV uses to gain insight in the sector as well as the criteria CFV uses to determine whether (and for how long) it has sufficient financial means to fulfill its tasks. Furthermore, the policy rules show the way CFV effectuates the BBSH (articles 5, 6, 12, and 31 in specific).

#### *Articles 9, 10 and 12: Contribution to CFV*

CFV gains its financial means by contributions on the corporations for the financial restructuring funds. CFV is allowed to determine the height of the contribution itself (based on the annual rentals of housing units), within specific limits. If CFV considers a corporation to have made significant contributions to activities in the name of, or on behalf of, other corporations, CFV has the right to remit from that contribution on the corporation. Other than strict financial restructuring, also the CFV organization is financed from this contribution.

### **DAEB-regulation**

For a long time, corporations executed their tasks being reimbursed by governments (local and nationals) and receiving subsidies for the developments of neighborhoods and housing. In European regulation, agreements have been made on the allowance of member states to (financially) support non-government organizations. These agreements on 'state aid' are included in the Treaty on the Functioning of the European Union, articles 106 and 107 (European Union, 2010).

The TFEU still allows governments to support 'services in the general economic interest' within boundaries. In Dutch, these services are named DAEB (Diensten van Algemeen Economisch Belang). The regulation on DAEB financing for corporations is currently written down in governmental decree named 'Tijdelijke regeling diensten van algemeen economisch belang toegelaten instellingen volkshuisvesting' (Rijksoverheid, n.d.f.). Relevant are especially the articles 2 (on services allowed), 3 and 4 (on reimbursement).

#### *Article 2: Social housing services in the general economic interest*

Article two of the governmental decree provides a list of services that corporations can consider DAEB activities. Amongst others, these include:

- Housing those who experience difficulties in finding housing (because of income or other conditions)
- Building housing with rents with a maximum height. So far, the maximum height of rents is based on the incomes on those earning less than the modal Dutch citizen
- Demolishment and selling of these houses
- Maintaining the local provisions
- Provide service directly related to the housing purpose
- Maintenance of crucial ownership in the neighborhood of housing (i.e. schools)

#### *Article 3 and 4: Reimbursement*

Reimbursement by the government is only allowed if housing corporations engage in activities of article 2, or activities that are closely related. Note that, as WSW guarantees are also considered state aid, this also holds for WSW guarantees. Furthermore, 90% of the housing units should be dedicated to people with a yearly income lower than €34.229. A corporation is to present and defend these numbers on its request for support.

In this respect, it is also only allowed for corporations to engage in rent contracts to their tenants when they have 'sufficiently accurate' insight in the income of the tenant. For special tenant groups (e.g. students) all types of exceptions are made.

#### **Hybrid sector structure**

By classifying corporations as social enterprises (Dutch: 'Maatschappelijke ondernemingen'), they can be considered as 'hybrid' organizations. Legally, corporations act entirely independent of the government, but at the same time the serving of public goals is their (statutory) reason of existence. As such, corporations act 'in between' the public and private world (Priemus, 2003).

By this hybrid structure, an attempt is made to combine the best of both worlds. Autonomous organization can use their expertise for the effective and efficient allocation of their resources, while the ministry is able to set the context in which corporations may operate and has the responsibility on realizing the social goals (AEDES, 2012a). However, this hybrid structure carries two core risks that are best explained in their extremes. First, corporation may be so independent, the government has no significant influence and, therefore, the responsibility of the minister is no more than phantasm. The second risk is that corporations are protected from the market to such an extent that they don't get (sufficient) incentives for effective and efficient allocation of their resources (Priemus, 2003).

## **Appendix VIII – Formal and informal institutional arrangements**

This appendix discusses the formal and informal institutional arrangements in place. This section first discusses the covenants established between CFV and WSW. Second the rules of participation of WSW are discussed. CFV policy rules are discussed third. Corporations are able to finance each other by what is named ‘collegial financing’. This peer funding arrangement is discussed fourth. Fifth, the governance code for corporations is elaborated upon. Sixth and final, the way regulators request their data at corporations is discussed.

### **Covenants CFV-WSW**

CFV and WSW established two covenants (CFV & WSW, 1998; CFV & WSW, 2000) that manage the so called seamless integration considering the financial security structures between the two organizations. Through the covenants, CFV and WSW ensure the existence of the following procedure:

When WSW identifies significant financial issues at a corporation, it will request the organization to take action itself. If this does not have the sufficient effect, WSW will order the corporation to apply for remediation support. Because of the covenant conditions on the ‘seamless integration’, in principle CFV approves this request for remediation. During this period, WSW can maintain its guarantees to a corporation when CFV makes a so called ‘decision of anticipation’. However, this requires a plan for remediation from the corporation, admitted by CFV. Remediation support can be given either as a subsidy or as a long-term liability. In practice, the ‘seamless integration’ is not seamless. As WSW mainly focuses on the cash flows and pledge, while CFV mainly focuses on the solvability (in their accountability judgments), their opinions on the financial stability of a corporation may differ (Hoekstra, Hoogduin, & Schaar, 2012). On solvability, CFV especially focusses on scenarios where the external climate ‘worsened’. Currently, CFV also includes cash flow prediction in their judgment. But still, in comparison to WSW, CFV uses equity more as a starting point. This is also because the goals of CFV and WSW differ (WSW, 2013). Where CFV is to check whether a corporation can fulfill its financial obligations, WSW acts more as a bank. In the current practice, cash flows often prove to be relatively ok while the equity positions are already decreasing. This corresponds to the idea that, in general, decline in the financial positions is mostly first seen in the equity positions before the cash flows (Kaplan & Schoar, 2005).

Good cooperation between CFV and WSW seems crucial for two reasons. Firstly, actions taken by WSW can greatly reduce the actions that need to be taken by CFV (Hoekstra, Hoogduin, & Schaar, 2012). In other words, WSW theoretically acts kind of like a ‘first line of defense’. In practice, WSW does so for temporary solutions, CFV often finances structural solution through its financial restructuring funds. In fact, this has even been used in the ‘promotion’ of WSW towards municipalities to secure their guarantees. Secondly, the other way around, CFV might benefit in their supervision from the data collected by WSW on individual corporations. However, this cooperation is not fully developed (Hoekstra, Hoogduin, & Schaar, 2012). WSW is not able to provide data to CFV, not even when this improves supervision, because of the rules of participation between WSW and the individual corporations. In order to share this information, written permission of the corporation is needed (CFV & WSW, 1998).

## Rules of participation WSW

When a corporation wants to make use of the services of WSW, it has to approve and sign the rules of participation. The rules of participation state under which conditions, for which purposes, what amount of money can be lend through WSW and other participating corporations, at what cost.

The loans guaranteed by WSW, are factually guaranteed in threefold. First of all, WSW has its own funds (financed by all participating corporations). Second, the loans are guaranteed by other corporations based on an 'outstanding loans' obligation (Dutch: 'obligoverplichting') to WSW. Third, WSW guarantees are backed by municipalities and the national government (WSW, 2007). This can be done in a number of ways (that we will not elaborate on), but all share one important notion: they are considered state aid. As such, WSW can only guarantee loans for a limited number of activities (i.e. the build and maintenance of 'social realty'). The exact possibilities are defined by ministerial decree (Rijksoverheid, 2010). Also, WSW 'only' provides guarantees when corporations they don't have any more resources for investment (WSW, 2007).

WSW identifies six categories of (a total of 40) corporation activities they may guarantee loans for. The way of categorizing varied a lot over the recent years, the type of activities basically remained identical. Here, we follow the most recent categorization (as it is in line with the ministerial decree). WSW can provide guarantees for 1) housing units, 2) investments in the livability as well as appurtenances belonging to 1), 3) social realty, 4) investments in the livability as well as appurtenances belonging to social realty, 5) inevitable activities related to 2) and 4), and 6) temporary shortages in liquidity (WSW, 2010).

Traditionally, each guarantee given by WSW is given to explicit investment expenditures of a corporation (CFV, 2012a). This was changed in 2007, by the introduction of the so called 'volume of facilitation': On basis of the expected cash flows and the pledge, WSW up front determines an amount of financing (in a maximum period of three years) it will guarantee (WSW, 2007). In this way, corporations are able to close bigger contracts at the best time possible. Obvious disadvantage is that corporations now have access to money even when they don't use it for investments. Even though this is not officially allowed, corporations used this opportunity on liquidity (e.g. to fulfill margin calls or engage in commercial activities) because of a lack of supervision on the spending of the money (Hoekstra, Hoogduin, & Schaar, 2012). Corporations often thought to use this liquidity only temporarily and 'replace' it by other financing means later.

This room for maneuver with the facilitation volume exists as the way the volume is determined on forehand is different from the way the 'performance' of the volume is determined later. The upfront determination of the volume is determined based on the cash flows, pledge, and planned activities. However, in the evaluation of the volume, less attention is given to the realization of activities. Instead, the main point of focus lies on whether the expenses has been made. On the income side, less attention is given as to how these income is realized, it may in fact come from the selling of DAEB equity. And as part of revenues from DAEB selling may be used for non DAEB activities, the current working of the facilitation volume may offer corporation the opportunity to engage in non DAEB activities even though WSW facilitation volumes cannot be used for that purpose.

By the guarantees of WSW, corporations are able to get low interest on their loans. As compensation, corporations pay WSW 0,0069% of their outstanding guarantees per quarter.

Corporation may also finance each other by 'peer funding' (more on this in the next paragraph). Over the peer funding loans corporations pay WSW 0,0023% per quarter (WSW, 2007).

Furthermore, as already noticed, corporations mutually guarantee each other through an obligation on their outstanding loans (when the central WSW fund is not sufficient). The amount depends on the amount of guaranteed loans a corporation has, with a maximum amount of 3,85% on the 'normal guarantees'. Some exceptions exist for variable loans and peer funding.

## **CFV policy rules**

On the basis of the Dutch housing law and BCFV, CFV each year publishes policy rules. Amongst others, these policy rules include the criteria used for financial supervision, policy on the financial restructuring and corporation contributions. As CFV is free to incorporate more elements in their policy, they also elaborate on their advisory function to BZK. All four elements are briefly discussed below.

### *Financial supervision*

CFV is the sector financial regulator. As such, CFV regulates on BMV, financial risk management and quality of the financial accountability products. To gather information, CFV is collecting a variety of documents to be provided by corporations through Corpodata (discussed at the end of this appendix) (CFV, 2008). Corpodata is functioning as intermediary between corporations and BZK, CFV and WSW since 2008 (CFV, 2009n). The information gathered by CFV yearly result in a continuity judgment and a solvability judgment (CFV, 2008; CFV, 2011). From 2013 onwards this changes to policy rules focused more on continuous judgment, having one formal judgment yearly (CFV, 2012ad).

In the policy rules, the criteria (including standard accounting terms as ICR, LTV, DSCR) to come to both judgments are extensively discussed. However, the norms are not mentioned. Apart from the degrees of freedom this brings the regulator, there is also a more basic notion to explain this. In their accounting, currently described by the RJ645 accountancy guideline, corporations have relatively many degrees of freedom. This hardens the regulation (including norm setting) of CFV as this reduces the comparability of corporations. The key indicator of indicator of interest that of the preservation of social capital. Although appearing a standard notion, the determination of it is not trivial. This is not in the last place caused by the degrees of freedom allowed by RJ645.

Also, the publication of data in sector reports is mentioned. Over the years, CFV published a number of reports. These include reports on the sector performance in terms of realization and the so-called CiP reports ('Corporatie in Perspectief'). CiP reports are made for each corporation individually. They benchmark the corporation performance on their geographic peers and peer types (CFV, 2010a) (e.g. specialized in care housing).

### *Advisory functions*

Apart from the financial regulation that is the core activity of CFV, CFV also advises the ministry on a number of different subjects. First, CFV advises on the legitimacy of corporations. This is especially relevant when new corporations enter the market (for example by a fusion between two corporations) or the status of a corporations are to be changed (CFV, 2008) (for example, by switch from 'vereniging' to 'stichting' as legal entity form). Also, CFV advises BZK on the social housing performance of corporations. More specifically it advises on the amount of selling of equity. This field

also includes advising on investments of a corporation abroad. CFV is fairly limited in its sanctioning possibilities. Hence, it also ‘advices’ (or actually asks) BZK to intervene in a specific way (CFV, 2011).

#### *Financial restructuring*

In case of financial distress, corporations may make a claim on the financial restructuring fund of CFV. The policy rules elaborately discuss the requirements and process needed to get financial support. It also discusses the responsibilities of the different actors involved in different stages of the claim. Most important here, is that a claim is only successful if it is clear that utilization of the corporations own ability to financially restructure is insufficient to become solvable again.

A caveat here is that a corporation is no longer credible by WSW standards (and, hence, loses its financing capabilities) though not in urgent problems according to CFV standards. It is this vacuum the CFV-WSW covenants operate in. In addition, CFV also has a so-called financing fund that may be utilized as bypass financing.

#### *Corporation contribution*

To finance support on corporations, CFV has the ability to put a levee on all (other) corporations in the Netherlands. For the financial restructuring, these corporation contributions are determined on the basis of the restructuring support needed. The cost are spread over the corporations on the basis of the annual rental revenues. The maximum contribution for a long time has been limited to 1% of the annual rental revenues per year (CFV, 2009n). However, this proved to be a weakness for the Vestia case. Hence, it has now been increased to a maximum of 5% (Ministerie van Binnenlandse Zaken en Koninkrijksrelaties, 2012). Each year, CFV published the total contributions gathered by corporations in its policy rules (CFV, 2012ad).

#### **Collegial financing**

Just after the financial autonomization of the sector, issues arose surrounding the excess of equity (Dutch: ‘vermogensovermaat’, i.e. amount of equity not needed for safeguarding continuity or the core social housing business) of corporations (CFV, 2002; Etty, et al., 2002). To limit this amount of excess equity, politics threatened with regulation on the sharing of tasks and responsibilities unless the sector would take action itself (Kempen & Co, 2003).

From this, structures of so called ‘collegial financing’ developed. As backbone of the financing of corporations, WSW also provided guarantees for these types of loans. Article 6 of the WSW rules of participation allow participating corporation to lend money to each other. Obviously, this goes at the cost of their own volume of facilitation. Only condition is that the terms of the loan should be exactly similar, only the interest percentage may be set lower (WSW, 2007).

#### **Governance code for corporations**

The governance code was made by Aedes and VTW as a joint effort to improve the quality of the internal supervision (Hoekstra, Hoogduin, & Schaar, 2012), as this was found to be not fully developed (Boer, Hooze, Biesheuvel, Meurs, Leeuwen, & Lensen, 2005; CFV, 2005). The overall opinion is that supervision as a whole can gain, when the internal supervision (of the supervisory board) and other checks and balances within corporations work effectively (Goodijk, 2012; Algemene Rekenkamer, 2008). The governance code provides guidelines to do this in a transparent way (Hoekstra, Hoogduin, & Schaar, 2012).



The code contains a number of principles on the topics of compliance, the executive board, the supervisory board, and the audit function. Each principle is made tangible by more specific provisions. We will here treat the most important elements of the governance code (Aedes & VTW, 2011).

Not every corporation is to comply with every provision of the code. However, when a corporation deviates from a code provision, they are to motivate that decision in their annual report. Furthermore, every change in the governance structure and code compliance is to be discussed with the supervisory board.

In the annual report, the executive board is to discuss the way the internal risk and control systems work, and how they are managed. Special attention should be given to the way the risk management on the undertaking of larger transactions is arranged. The executive board will also construct an assessment framework for investment decisions. This framework is to be approved by the supervisory board.

The supervisory board supervises the functioning of the executive board. In that perspective, the supervisory board will, amongst others, focus on the strategy and risks of the respective corporation, the structure and working of the risk control systems, the risks taken by (larger) investments, and the financial reports. Also, the supervisory board is empowered to hire the corporations external accountant needed for the formal financial statements (in practice, it often does this based on the advice of the executive board).

In the audit, a difference can be made between the internal accountant/auditor (responsibility of the executive board) and the external accountant (supervisory board). The external accountant (and, if applicable, an audit committee installed by the supervisory board) is involved in determining the works of the internal accountant, apart from its activities on the financial reporting. The formal task of the accountant is arranged by law and further specified by (obligatory) guidelines from the Council for the Annual reporting (Dutch: 'Raad voor de jaarverslaggeving') (Ortec, 2012). The specific corporation guidelines are found in guideline 645 (Deloitte, 2011).

### **dPi/dVi data requests**

Through Corpodata, the ministry of BZK, WSW and CFV receive data twice a year. Before the first of February, corporations hand in prospective information in the dPi (Dutch: 'de prospectieve informatie' (Corpodata, n.d.b)). Before the first of July, information on the accountability is to be handed in, known as the dVi (Dutch: 'de verantwoordings informatie') (Corpodata, n.d.c). Both the dPi and dVi data are to be accompanied by board statements. In case of the dVi, also assurance reports, financial statements and an accountancy statement is required in addition (Corpodata, n.d.c).



Not all information gathered by Corpodata is shared with all three requesting organizations. WSW asks its members for some specific data, as does CFV (Corpodata, n.d.b; Corpodata, n.d.c). The majority of information, however, is shared across all three organizations. The data that is requested by BZK and CFV is specified in the appendices of the BBSH (the BBSH is discussed in appendix VII). This distribution of gathered data is schematically represented in figure VIII.1.

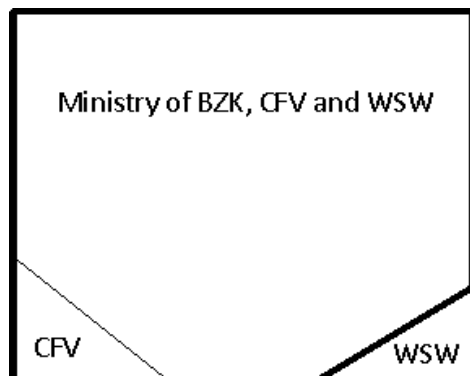


Figure VIII.1: Schematic representation of the division of gathered data.  
The accentuated box represents data fields specified in BBSH

## Appendix IX – Actors and Games

This section focuses on the actors involved in the regulatory regime and their mutual relations and capabilities. In the first paragraph, the actors involved in the regulatory regime of corporations are discussed. The more formal connections of the network in which the actors operate is schematically sketched in the second paragraph. Subsequently, tensions in the actor network are elaborated on in the third paragraph.

### Actors descriptions

This paragraph provides a general description of the actors involved in the regulatory regime of the Dutch social housing sector. Actors are elaborated upon in alphabetical order.

#### Accountant

The accountant (i.e. auditor) is responsible for the quality and correctness of the financial statement. This statement, guided by an accountancy statement, is subsequently used by both the supervisory board as well as CFV. In preparing the statements, the auditor has to follow the guidelines of the Council for Annual Reporting (RJ645) (Ortec, 2012). Figure IX.1 shows the distributions of accountants of the housing corporations over the period 2005-2011. It must be noted that some accountants are working for smaller corporations (e.g. BDO), while some work for bigger (e.g. KPMG). This can be deducted from comparing figure IX.1 to figure IX.2, as figure IX.2 shows the market shares of accountants based on the number of housing units (CFV, 2012c).

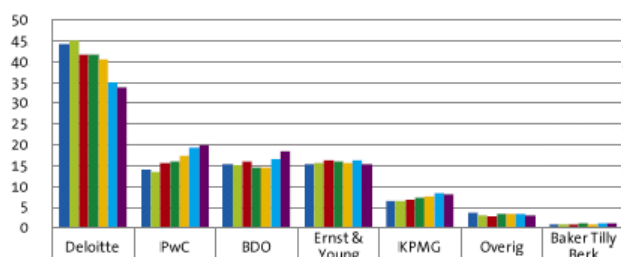


Figure IX.1: Accountant market share (%) on corporations

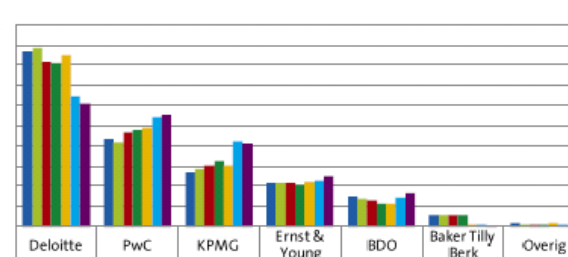


Figure IX.2: Accountant market share (%) on housing units

Both CFV and WSW rely quite heavily on the work of accountants. In the recent history, CFV doubted a number of times on whether accountants performed their jobs (as determined by law) correctly. Simultaneously, AFM itself got more involved with the accountants sector as it was appointed as their regulator/quality controller. For that reason a covenant between CFV and AFM was set up to be able to determine low quality (or even fraudulent) reports quicker (AFM & CFV, 2012)

#### Aedes

Aedes is the branch organization of the Dutch housing corporations, representing the interests of housing corporations in The Hague and Brussels. Aedes has three points of focus: advocacy, bonding of members, and services. In itself, Aedes is not organization involved in the monitoring of corporations (Schilder, Mosch, & Hage, 2006). However, through its services pillar, Aedes contributes something, especially the internal, monitoring activities. Aedes was a driving force between the industry code (Aedes, 2002), the training program 'professional supervision' for supervisory board members (Schilder, Mosch, & Hage, 2006), and the governance code for housing corporations (Aedes, 2011). About 95% of the Dutch housing corporations is member of Aedes. As disciplinary sanction, a corporations membership of Aedes can be (temporarily) suspended (Aedes, 2012b).

### *BZK (Ministry of the Interior and Kingdom Relations)*

Since 2010, the supervision on the legitimacy, governance and integrity of corporations is done by the DG housing (Dutch: 'Directoraat-generaal Wonen, Bouwen en Integratie) of the Dutch Ministry of the Interior and Kingdom Relations (BZK). This is done on the basis of annual reports, retrieval of data of corporations (through Corpodata) and auditor statements. By the legal obligation on the approval of changes in the statutes of corporations, the Ministry ensures that the interest of public housing is enshrined in the very foundations of the corporation. Also the supervision on public housing performance is done by the DG housing. This supervision is partially based on findings of CFV and field signals (e.g. from municipalities). Its findings on sector performance are yearly reported to parliament (Hoekstra, Hoogduin, & Schaar, 2012). Before 2010, similar supervision was performed by VROM (Schilder, Mosch, & Hage, 2006).

### *CFV*

By law (Rijksoverheid, n.d.e.), the minister of BZK delegated two activities considering financial supervision to CFV: data gathering and judgment. So, CFV has no rights to intervene (except to secure quality information). In practice, CFV has slightly more powers it can exceed that relate to quality information or because it is capable of threatening with BZK intervention. In case of limited financial problems, CFV asks corporations to come up with a plan of action. In case of more stringent problems, CFV requests the Minister of BZK to use his competences.

CFV judgments traditionally focussed on financial consequences in terms of continuity of (individual) corporation policies. Therefore, CFV judges the corporations on the current capital (the solvability judgement) as well as proposed future activities (the continuity judgement) (Hoekstra, Hoogduin, & Schaar, 2012). Currently, CFV focuses on 6 points in the same two judgements: quality of the financial information, the maintaining of social capital, risk management, liquidity, solvability, and continuity (CFV, 2012d).

Apart from supervision, the CFV also functions as restructuring and project funds. CFV is, by law, financed by the corporations themselves. The function was brought to life in 1988 to prevent corporations from bankruptcy. This, again, had three main reasons: ensure stability to external financiers and occupants as well as preventing capital leakage (Hoekstra, Hoogduin, & Schaar, 2012). The downside, obviously, is that moral hazards may now occur.

### *Corpodata*

Corpodata is a joint cooperation between CFV, WSW and the DG housing (BZK). Through Corpodata, these organizations jointly request financial information as well as information on the housing performance of corporations. Corpodata is responsible for the data retrieval and its spreading to the relevant organizations. Corporations have two deadlines for delivering data to Corpodata. For the prospective information (dPi) the deadline is the first of February, where the deadline for the accountability information (dVi) is the first of July (Corpodata, n.d.a).

Corpodata also acts as first in line in the data processing. If corporations supply information wrongly, or with 'extreme' values, Corpodata checks with the corporation whether the information supplied is as intended. Apart from the identification of typos, this repeatedly also resulted in corporations adapting the data they provide. Corpodata has no formal legal status.

### *Corporations*

In 2002, the Netherlands counted 552 housing corporations (CFV, 2003). Because of mergers, the number of corporations dropped to 389 in 2012. Together, these 389 corporations operate a near 2,5 million housing units, almost a third of the total Dutch supply. The total Dutch social housing sector then has an operating value of nearly € 108 billion, with over € 34 billion of social housing equity (based on exploitation value) (CFV, 2012b).

On average, a corporation holds just over 6200 housing units (CFV, 2012b). However, there are big differences between corporations. The 50 biggest corporations own about half of the total amount of housing units owned by corporations (Schilder, Mosch, & Hage, 2006). For example, Ymere owns over 85.000 housing units (Ymere, 2012), where Veron owns 185 housing units (CFV, 2012e). What all corporations have in general is that they are headed by an executive board. The executive board is supervised by a supervisory board.

### *Municipalities*

As municipalities often act as the contracting authorities for corporations, they also play a role in the supervision of corporation. However, this role is quite complex. Over time, corporations were more and more allowed to undertake activities in the 'non-DAEB domain', e.g. building more expensive housing units, or housing units build for sale. This gave a dual role in respect to the municipalities as corporations now had to negotiate for cheap ground for both types of activities.

Furthermore, the goals of the municipalities itself are also ambiguous. Though in the core the role of the municipality is to establish a housing plan (that, in practice, is often co developed with a corporation), the municipality is also attracted to the commercial activities and has a benefit from doing profitable business. Even if this does not contribute to the housing performance of that municipality. For example, most municipalities are attracted to the idea of having a successful industry area. This will often blurs their judgment as the development of an industrial area when each surrounding municipality already has one (which is actually often one of the arguments to also develop an area), it is less likely to be successful.

On top of that, it appears municipalities have a hard time to evaluate the social performance of corporations. Therefore, it is argued that a more binding relationship between corporations and municipalities is needed (Boer, Hooze, Biesheuvel, Meurs, Leeuwen, & Lensen, 2005).

### *SVWN (Foundation for the visitation of housing corporations in the Netherlands)*

SVWN was founded in 2009 and has the goal to develop, manage and safeguard an objective and independent system for the visitations of housing corporations. It was founded by the national government, Aedes, VTW and VNG. It is pure sector initiative, not backed by the government.

Although SVWN is founded only in 2009, there is a longer history of visitation of housing corporations in the Netherlands. The idea was first mentioned by Aedes in 1999. Further research by the committee Sas (in 2005), the audit council (2005-2008) and SEV (2008-2009) resulted in the foundations of SVWN.

A corporation should undergo a visitation at least every four years. In the period between 2007 and 2011 around 80% of corporations had visitations. The other (smaller) corporations were exempted till March 2012. Almost all visited corporations score according to the norm. However, bigger corporations seem to do it slightly better than smaller corporations, especially on the 'governance' criterion (TU Delft, 2012). SVWN itself does not perform visitations, it provides accreditations for

organizations to perform visitations and checks visitation on the correct application of the developed methodology (SVWN, n.d.).

#### *VTW (Association for supervisors of housing corporations)*

VTW is founded in 2002 as a professional body for those responsible for the internal governance of housing corporations. VTW has around 1600 member that are member of the supervisory boards of over 320 housing corporations. VTW sees itself as a centre of expertise and knowledge and has the goal to contribute to a strong, independent and professional internal governance of housing corporations. For this reason organizes discussions, workshops etcetera, and cooperates with organizations as Aedes, CFV and BZK (VTW, n.d.).

#### *WSW*

Through WSW, housing corporations are able to borrow money at favourable interests by providing guarantees to the financiers. This is done by having an outstanding reserve (Dutch: "Obligo reserve") in the sector and backing of national and regional governments. The guarantees made by WSW gives financiers the security on their loans (WSW, n.d.a). WSW has a risk equity of € 485 million and an outstanding reserve at corporations of € 3,2 billion. At the end of 2011, WSW stood deposit for over € 86 billion. 96% of the corporation participate with WSW (WSW, 2012). WSW is a private initiative, but because of the backing by government bodies any loan provided by WSW is considered state aid. Hence, it depends on the nature of a loan whether WSW is allowed to stand deposit. Unique is that through the outstanding reserve, corporations can be obliged to financially contribute in the loans of other corporations.

### **Actor network dependencies**

Supervision takes place in complex networks. This paragraph elaborates on the structure of this network. Therefore, first the distribution of financial security functions is closer looked at, before mapping the relations between actors.

#### *Financial security functions*

Executive boards of corporations discuss financial performance with their supervisory board. Also the (external) accountancy statement is used as input in this discussion. The accountancy statement is also important input for the supervision of CFV, together with the data it receives from a corporation through Corpodata. The result of the data analysis by CFV is communicated back to the corporation, but may also be communicated to the ministry. In practice, this latter is mostly the case when (serious) financial issues are existent. The ministry also receives corporation specific financial data, but is not actively using this 'raw' data for financial supervision purposes. Furthermore, WSW uses financial data to determine the facilitation volumes and monitor their guarantees. Also, housing corporations that are member of AEDES are obliged to do a visitation at least once every four years.

Based on data of all corporations together, CFV and the ministry also provides market reports it sets out in the network. The reports of CFV are, logically, more financially focusses where the ministry focusses more on the housing performance and corporation governance.

Apart from CFV and WSW monitoring the financial status of corporations, they also provide financial backing in case of financial distress. Both therefore have access to a funds that is filled mainly by corporations themselves. In their financial security functions, both WSW and CFV are backed by the

national government. The guarantees on loans made by WSW are partially also covered by municipalities in which the corporation operates.

For supervision, one can differentiate between internal and external. The internal supervision is one of the core tasks of the supervisory board. To perform this task, the supervisory board has means to intervene in (the operations of) the executive board. External supervision on financial issues is formally done by CFV. However, CFV has no formal means for intervention, but is dependent of the ministry. The content of this subparagraph is schematically represented in figure IX.3.

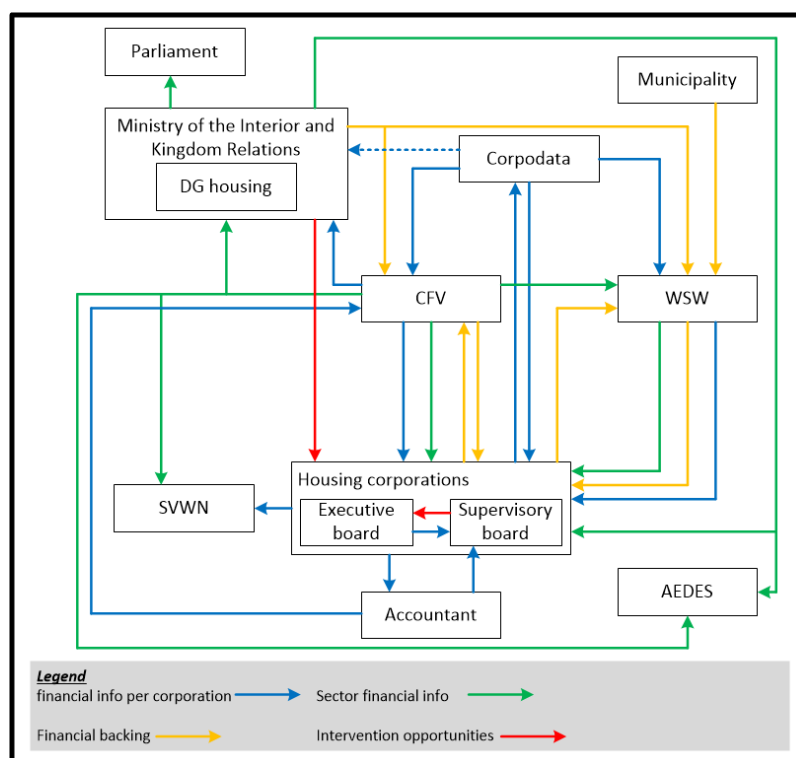


Figure IX.3: Schematic representation of the financial security functions

### Actor relations

In this subparagraph, the relations between actors in the 'corporation network' are elaborated on further. These relations are schematically shown in the formal chart of figure IX.4.

In the previous subparagraph the roles of CFV, WSW, SVWN and the accountant on the external supervision were already discussed. Addition that we have to make here, is the existence of a covenant between CFV and WSW to align their activities. External supervision is also performed by the ministry, municipalities and citizens (i.e. tenants). The ministry formally supervises on the integrity of corporations as well as the social housing performance. Municipalities and tenants have no formal role in supervision, but are capable to do so through their client relation with the corporation (e.g. using performance contracts). It appears, however, this is

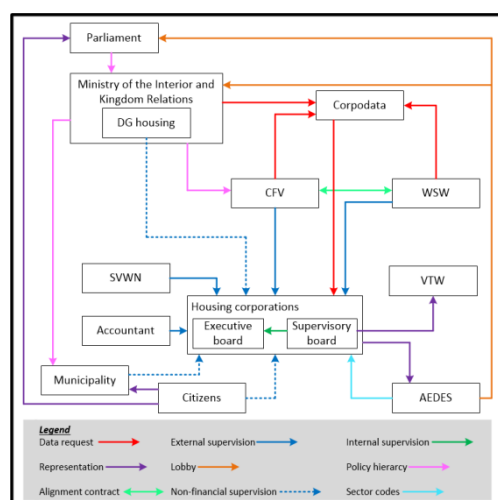


Figure IX.4 - Actor relations

rarely done efficiently (Hoekstra, Hoogduin, & Schaar, 2012; Schilder, Mosch, & Hage, 2006).

Citizens are represented in the municipal council and parliament. Through regulation, parliament can control the (responsibility of) supervisory tasks and activities of municipalities, the ministry and CFV. Housing corporations are represented by the sector organization AEDES, who actively lobbies in The Hague. There is a separate organization from bringing supervisory boards of corporations together: VTW. The ministry, CFV and WSW collect their corporation data through Corpodata.

## Network tensions

In the network described above, multiple battles are fought (or, more softly, games are played). These tensions are described in this section. First and foremost, the monitoring procedure between corporations and CFV is discussed. In the second paragraph, the role of WSW in the financial supervision is elaborated on. Subsequently, the third paragraph describes the relation between WSW and CFV. The tensions between corporations and the municipalities and corporations and accountants is described in the fourth and fifth subparagraph respectively. The sixth subparagraph elaborates on relations amongst corporations themselves. Concluding, the seventh subparagraph will shortly elaborate on the more internal relation between the executive and supervisory board.

### *Corporations vs. CFV*

Each corporation submits (through Corpodata) data to CFV twice a year. Before the first of February, corporations are to hand in their plans (approved by the supervisory board of the corporation) on the activities they plan to undertake in the next five years (dPi). Based on these plans, CFV judges whether it thinks the proposed activities match the equity position of the corporation. From 2008 to 2010, it was also possible a corporation would get a so-called C-judgment, indicating the proposed activities were insufficient in respect to the equity position of the corporation. In other words, the corporation has an excess of equity and should invest more of its equity (Schilder, Mosch, & Hage, 2006).

Before the first of July, corporations are to hand in financial performance data on the previous year (also approved by the supervisory board of the corporation), accompanied by the report of the external accountant (dVi). It is based on this information that CFV judges on the solvability of a corporation (Hoekstra, Hoogduin, & Schaar, 2012).

More accurately, the dVi and dPi information are used as sources of information, together with earlier experiences of the DA (district advisor), in desk research for a preliminary judgment of the corporation. When the preliminary judgment is ok, this also holds as the final judgment. In case the preliminary judgment is not ok, CFV will engage in a procedure of 'further research'. During this period the DAs will gather extra data (e.g. WSW judgments) and discuss findings and considerations with the respective corporation. Second goal of this contact is to gain extra information from the side of the corporation (CFV, 2009; CFV, 2012d).

In case of limited concerns/issues, CFV will ask the corporation to come up with a recovery plan, based on which a monitoring agreement is made. The monitoring agreement is included in the final judgment. In case of more serious issues, CFV might place a corporation under 'intensified supervision' to keep a closer eye on a corporation's performance. In case of serious financial issues that are not (sufficiently) recognized by the executive and/or supervisory board, i.e. are (often) related to governance issues, CFV might ask the Minister of BZK to intervene (Hoekstra, Hoogduin, &

Schaar, 2012). The corporation will have a negative final judgment of CFV. Within three months, the corporation has to hand in a recovery plan that gives insight in whether there can be sufficient recovery (CFV, 2009).

The process of financial supervision is schematically shown in figure IX.5. What is not depicted in the figure, and neither told above, is that, generally, a single DA manages the account, monitoring agreements, and final judgment of a corporation. Since 2011, DAs attempt to visit at least the biggest group of corporations in duos. Factually, it is so that only if the dVi or dPi preliminary results raises flags, and the DA chooses to ignore these flags, he will have to be authorized by his manager.

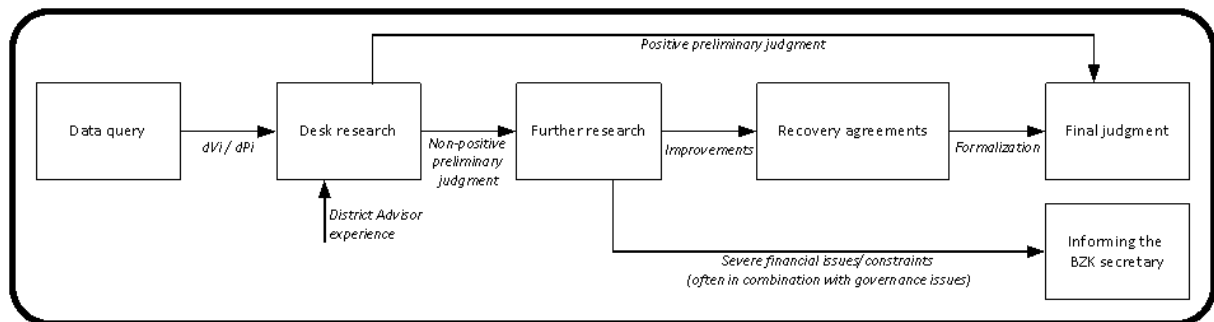


Figure IX.5: Schematic representation of the financial supervision process

In first instance, figure IX.5 may suggest the supervision process is a relative unilateral process. A closer inspection, however, learns this is not the case. First of all, it is the corporation itself that hands in the information in the data query. Furthermore, when applicable, a corporation is actively involved in the further research and making of recovery agreements because of the adversarial principle. This makes that only the desk research is done internally at CFV, creating the paradox that only a positive final judgment ‘can come as a surprise’. This shows, the financial supervision of a corporation actually is a bilateral (though not equal) effort of CFV and the corporation itself.

### Corporations vs. WSW

Although WSW is not a formal regulator, it performs important supervisory tasks. It does so in order to monitor and control the status of its guarantees on loans. It is therefore, that WSW also makes use of the dPi and dVi of Corpodata, thereby making the financial supervision of corporations a multi issue that is further discussed later in this appendix. But WSW has a second goal with this retrieval of data. It is on the basis of this information that WSW determines the corporation’s facilitation volumes (Hoekstra, Hoogduin, & Schaar, 2012). The WSW judgment is, in its essence, a less adversarial process than the supervision of CFV. WSW is a foundation that has to let most decision be approved by a council of participants. This makes that corporations have a certain ability to determine on what aspects they are controlled (WSW, n.d.b). Still, the main aspects of WSW control are similar to that of other regulators (like CFV), shown by the fact that WSW retrieves almost the exact information as CFV and BZK do from the dPi and dVi (Corpodata, n.d.b; Corpodata, n.d.c).



### *Corporations vs. CFV & WSW*

In appendix VII, the covenant between CFV and WSW that is to establish the so-called ‘seamless integration’ was discussed. It was found, that the integration is not as seamless as it appeared to be. Neither the cooperation between CFV and WSW is fluently, as WSW is often not allowed to share corporation specific information with CFV because of its rules of participation.

Over the years, there has been a lot of discussion on how to structure the regulatory regime considering housing corporations. Some argued that all supervision should be done by WSW (Boer, Hooge, Biesheuvel, Meurs, Leeuwen, & Lensen, 2005), while others argue all supervision should be bundled within CFV (Schilder, Mosch, & Hage, 2006). Again others, suggest a way in between, or the installation of a third organization (Hoekstra, Hoogduin, & Schaar, 2012). This constantly changing views create a kind of tension between CFV and WSW. CFV now only work together in their retrieval of data (through Corpodata) and the remediation of corporations, but not in a structured way in the ‘regular’ supervision process (this is strongly dependent on the relation between the CFV DA and the WSW account manager), though there are periodic board meetings. For corporations this also creates confusion as it is possible that CFV judges the solvability and continuity position of a corporation as insufficient, while the corporation is able to attract extra external financing because of the WSW judgment.

The difference in judgment is often explainable because of the different goals of CFV and WSW. Still, this is often not clear in the communication to a corporation. This problems seem to be bigger when the CFV judgment is more negative compared to the judgment WSW than vice versa. Even though the goals are different, some elements are similar (and could thus be better aligned). Also, it may help if both CFV and WSW are aware their judgments differ before communication to the corporations.

### *Corporations vs. municipalities*

Also municipalities have an important role, as they mostly act as client to corporations. This relationship is quit complex. On the one hand, corporations negotiate with municipalities on affordable grounds for the development of DAEB approved social housing. On the other hand, corporations negotiate on ground for the development non-DAEB activities simultaneously (Schilder, Mosch, & Hage, 2006).

Furthermore, the goals of the municipalities itself are also ambiguous. Though in the core the role of the municipality is to establish a housing plan (that, in practice, is often co developed with a corporation), the municipality is also attracted to the commercial activities and has a benefit from doing profitable business. Even if this does not contribute to the housing performance of that municipality. For example, most municipalities are attracted to the idea of having a successful industry area. This will often blurs their judgment as the development of an industrial area when each surrounding municipality already has one (which is actually often one of the arguments to also develop an area), it is less likely to be successful.

On top of this, it is also municipalities that try to involve corporations in their plans. Over the years, municipalities are experiencing more and more financial stress, while they see (‘their’) corporation having strong equity positions (Hoekstra, Hoogduin, & Schaar, 2012). Municipalities therefore also seduce corporations for the development of shelters for the homeless, nursing homes and daycare facilities for example, in order to improve the livability of a neighborhood (Gemeente Rotterdam,

2010). Altogether, this dynamic and complex relation between municipalities and corporations hamper the supervision a municipality can perform on the basis of its client status (Schilder, Mosch, & Hage, 2006).

#### *Corporations vs. accountants*

A corporation has to let its yearly financial statements be approved by an external accountant. The financial statements and accountancy statement are the prime sources of information for the regulatory agencies. Accountants have to follow guidelines in their representation of the financial figures. Still, these guidelines allow for variation in valuation and assessment of risks (Hoekstra, Hoogduin, & Schaar, 2012). Obviously, a (executive board of a) corporation will want to use this leverage. This brings a tension in the relation between the corporation and the accountant.

In principle, it is the accountant who is in dubio between rightfully performing its job and satisfying his client. Vestia is one of the cases that shows this (Hoekstra, Hoogduin, & Schaar, 2012). Considering this vulnerability, regulatory agencies are to (also) closely monitor the quality of the financial statements and accountancy statement.

#### *Corporations vs. corporations*

After the financial autonomization, corporations are more and more considered competitors of each other. To some extent, some chief executives of corporations try to honor this point of view. However, they rarely do so in terms of social housing performance (i.e. in terms of BMV – the preservation/growth of social capital). This is also because of the (formal) leading role of the municipality in this respect. Therefore, corporations mostly tend to show their capabilities and power by their engagement in all types of other activities.

In reality, not much competition is present. Corporations act in a system of mutual guarantees and collegial financing. On top of that, most corporations act in a quite well geographical demarcated area. Within this area, multiple corporations might be active. Still, probably by historical inheritance, it appears there barely is competition between these corporations either.

#### *Executive board vs. supervisory board*

Also within corporations there are tensions. In fact, many of these tensions are desired and known as ‘internal governance’ and/or ‘internal checks and balances’. In this subparagraph, attention is limited to the relation between the supervisory board and the executive board. In fact, here, the focus lies on the internal tensions in the tasks of the supervisory board in its relation to the executive board.

(Members of) the supervisory board generally have four types of functions (Lückerath-Rovers, 2011). First, they formally are the employers of the executive board. Second, they often act as advisors to the executive board, while they, thirdly, also are to monitor the executive board. Fourth, and non-formal, members of supervisory boards are often used because of their networks. In performing their tasks, tensions exist between these functions. Most obviously between the role of advisor and supervisor. Where in the role of advisor the relation to the executive board is to be built on trust, in the role of supervisor it is more based on alertness. This makes that there is a continuous game going on between the executive board and supervisory board in balancing these functions (Lückerath-Rovers, 2013).

## Appendix X - Basic information Servatius

### Overview

Servatius is a corporation active in the Maastricht area, operating just under 12.000 housing units. Servatius is the second largest corporation in the region. Together with the Woonpunt corporation, it operates over 75% of the corporation housing units in the region (figure X.1).

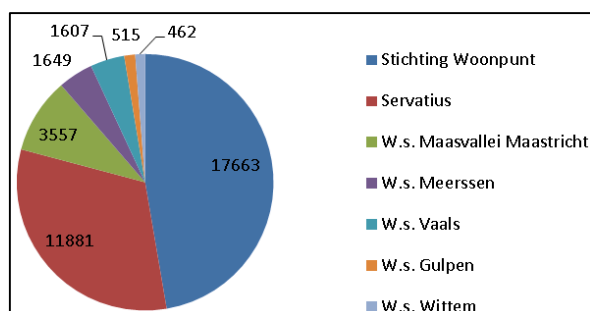


Figure X.1: Regional market shares of Servatius (based on #vhe in 2011)<sup>1</sup>

Servatius mainly owns family houses, complemented by 'low build' (i.e. four floors or less) apartments (figure X.3). Over half of the Servatius housing units were built before 1970. The biggest group since then (almost 20%) was built between 1980 and 1989 (figure X.2).

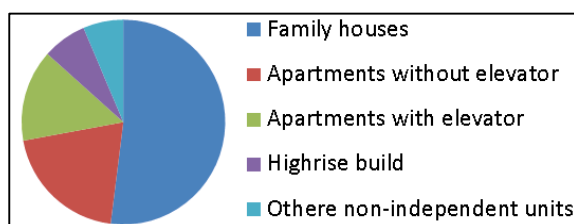


Figure X.3: Distribution to type on Servatius housing units (CFV, 2012f)

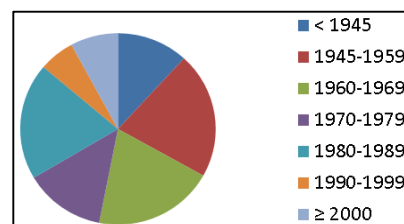


Figure X.2: Distribution to age of Servatius housing units (2011) (CFV, 2012f)

Being a social housing corporation, Servatius serves a public goal that does not allow for leakage of social capital. In the period previous to 2010, Servatius experienced multiple big (partly) commercial projects. Biggest, and most well-known, is that of the new campus of the Maastricht University which cost Servatius over €75 million (PCO Advies, 2010). The financial setback of the campus project and other projects forced Servatius to cut their social capital from 23,6% of their total balance capital in 2009 to 14,3% in 2010 (figure X.4<sup>2</sup>). That Servatius in 2010 and 2011 also underperformed to the (regional) market is visualized in figure X.5<sup>3</sup>.

<sup>1</sup> Based on (CFV, 2012f; CFV, 2012g; CFV, 2012h; CFV, 2012i; CFV, 2012j; CFV, 2012k; CFV, 2012l)

<sup>2</sup> Based on (CFV, 2012f; CFV, 2011a; CFV, 2010b; CFV, 2009a)

<sup>3</sup> Based on (CFV, 2012f; CFV, 2012g; CFV, 2012h; CFV, 2012i; CFV, 2012j; CFV, 2012k; CFV, 2012l) and (CFV, 2011a; CFV, 2011b; CFV, 2011c; CFV, 2011d; CFV, 2011e; CFV, 2011f; CFV, 2011g)

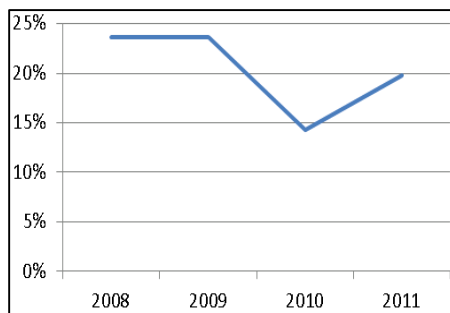


Figure X.4: Servatius social capital 2008-2011 (as % of total balance capital)

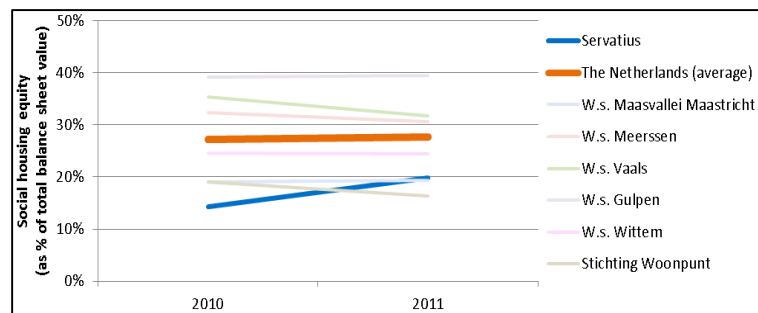


Figure X.5: Servatius social capital 2010-2011 compared

## Corporation profile

Before 2008, Servatius is known as an active corporation with an active director (Leks Verzijlberg). Verzijlberg is known as a social entrepreneur who often acts on the boundaries of the law. Liking to take care of things personally, he is awarded as the Maastricht ‘social housing provider with a vision’. Downside of his personal involvement is a lack of transparency throughout the organization (PCO Advies, 2010). Servatius had multiple of legitimacy issues with VROM, the Dutch ministry in charge of housing corporations at the time. An (afterwards) internal evaluation of the supervisory board of Servatius also brought to light a number of issues in the internal governance (IFO, 2010). Furthermore, the targets set by Servatius were considered too ambitious (PWC, 2011).

In 2008, the solvability position of Servatius was insufficient to CFV standards (CFV, 2009a). Also, the financial statements of Servatius were not approved because of a number of uncertainties. It turned out that Servatius, apart from the university campus project, was involved in over 80 highly complex and non-transparent projects that lacked an exit strategy and no proper risk control. In 2008, this contributed to a loss of €100 million on the university campus project (Servatius, 2009). The exit of the university campus project in 2009 did then cost €60 million (Servatius, 2010b) and an extra €15 million in later periods (PCO Advies, 2010). In the end, Servatius did not have to address CFV for support on the financial restructuring. However, the issues came at significant cost of the social capital, as was already shown in figure X.4.

## Appendix XI – Basic information Eigen Haard

### Overview

Eigen Haard is a corporation active in the Amsterdam area, operating 56.142 housing units. Eigen Haard is the third largest corporation in the region. Together with Ymere and Alliantie, it operates two thirds of the corporation housing units in the region (figure XI.1).

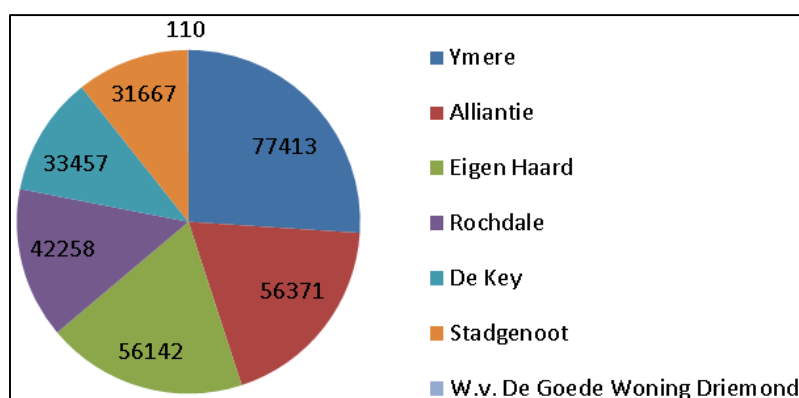


Figure XI.1: Regional market shares of Eigen Haard (based on #vhe in 2011)<sup>4</sup>

Almost two thirds of Eigen Haard real estate concerns ‘low build’ (i.e. four floors or less) apartments (figure XI.3). Around half of Eigen Haard housing units were built before 1970. The biggest group since then (almost 25%) was built between 1980 and 1989 (figure XI.2).

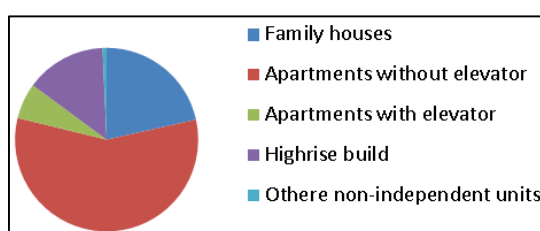


figure XI.3: Distribution to type on Eigen Haard housing units (CFV, 2012m)

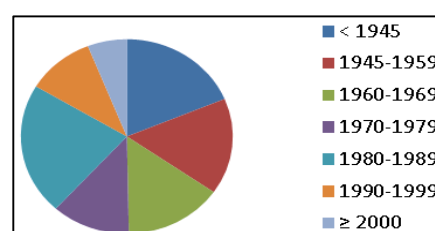


figure XI.2: Distribution to age of Eigen Haard housing units (2011) (CFV, 2012m)

The financial crisis also had its effect on the social capital of Eigen Haard (figure XI.4)<sup>5</sup>. However, Eigen Haard recovered and is doing significantly better than most other corporation in the region of Amsterdam (figure XI.5)<sup>6</sup>. In fact, many other Amsterdam corporations are under intensified supervision (Ymere, De Key and Stadgenoot) or faced scandals over the recent years (Rochdale) (Ministerie van Binnenlandse Zaken en Koninkrijksrelaties, 2013a).

<sup>4</sup> Based on (CFV, 2012m; CFV, 2012n; CFV, 2012o; CFV, 2012p; CFV, 2012q; CFV, 2012r; CFV, 2012s)

<sup>5</sup> Based on (CFV, 2012m; CFV, 2011h; CFV, 2010c; CFV, 2009b)

<sup>6</sup> Based on (CFV, 2012m; CFV, 2012n; CFV, 2012o; CFV, 2012p; CFV, 2012q; CFV, 2012r; CFV, 2012s) and (CFV, 2011h; CFV, 2011i; CFV, 2011j; CFV, 2011k; CFV, 2011l; CFV, 2011m; CFV, 2011n)

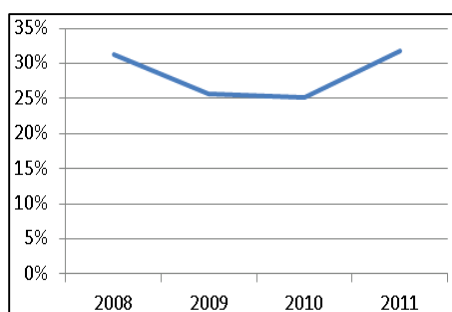


Figure XI.4: Eigen Haard social capital 2008-2011 (as % of total balance capital)

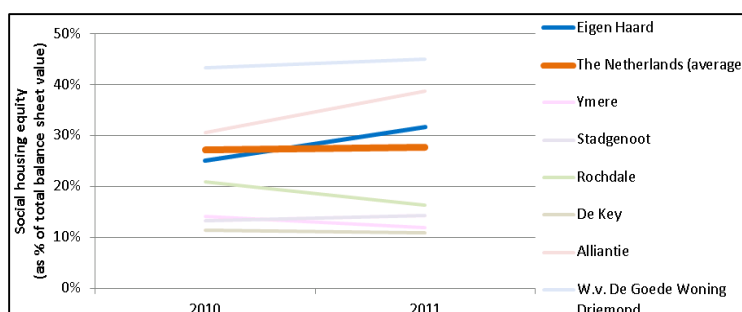


Figure XI.5: Eigen Haard social capital 2010-2011 compared

Eigen Haard is known as a corporation that, amongst others, actively engages in projects and ground positions. While many other corporations (in the Netherlands, but also in the growth region of Amsterdam) experienced significant cuts in their social capital, Eigen Haard managed to do reasonably well.

Though improvements are possible, Eigen Haard is considered a corporation that is aware of its actions. In contrast to some other corporation, Eigen Haard has a clear vision, strategy and plan of approach for the development of neighborhoods. Nevertheless, Eigen Haard also engaged in some quite expensive projects. However, in these cases Eigen Haard let its decision (processes) be evaluated by external parties. All in all, this gives the idea that Eigen Haard is in control of its organization.

However, in the role of peer monitor Eigen Haard seems less successful. Multiple of its direct geographic peers are under intensified supervision. On top, based on size, Eigen Haard falls in the same category as Vestia belonging to the biggest corporation in the Netherlands. Hence, one could expect the two also have some sort of contact with each other. However, Eigen Haard has to contribute over € 16 million for the financial restructuring of Vestia.

## Appendix XII – Basic information WSG

### Overview

WSG is a corporation active in the Breda area, operating just over 4.000 housing units. WSG is a middle sized corporation in the region (figure XII.1). The type of property of WSG widely varies (figure XII.3). However, over the last couple of years WSG is focusing more on care housing.

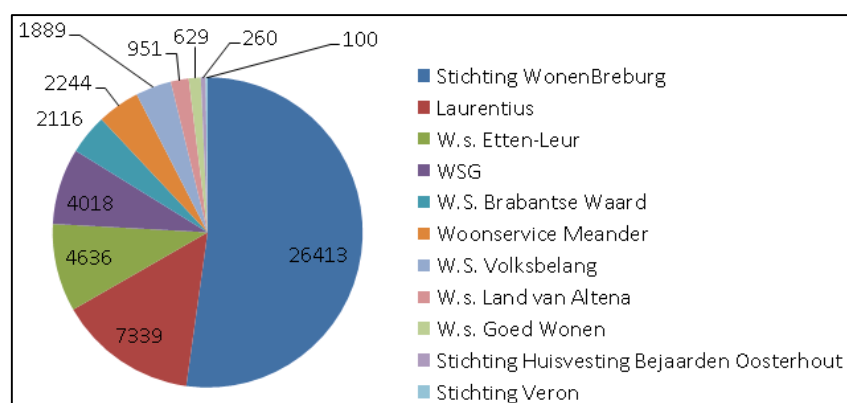


Figure XII.1: Regional market shares of WSG (based on #vhe in 2011)<sup>7</sup>

WSG had the ambition to almost double in size in just 5 years. To finance this growth, the older property was sold. As a result, more than half of the current property consists of property was built after 2000 (figure XII.2) at the cost of older property.

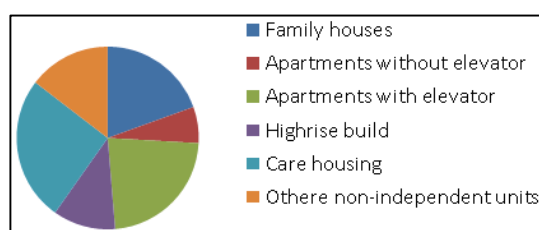


Figure XII.3: Distribution to type on WSG housing units

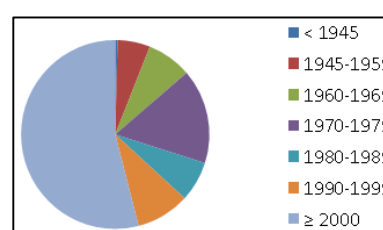


Figure XII.2: Distribution to age of WSG housing units (2011)

Because of the equity involved with expansion, the drive of expansion WSG had was normally unrealistic. This manifested during 2010, when WSG was forced to make a request on financial restructuring support of CFV. Also this came at the cost of WSGs social capital. WSG clearly underperformed to the region (visualized in figure XII.4)<sup>8</sup>. As there WSG has no (accountant) approved financial statements since 2010, WSG data is only available till 2009.

<sup>7</sup> Based on (CFV, 2012t; CFV, 2012u; CFV, 2012v; CFV, 2012w; CFV, 2012x; CFV, 2012y; CFV, 2012z; CFV, 2012aa; CFV, 2012ab; CFV, 2012ac)

<sup>8</sup> Based on (CFV, 2012t) (CFV, 2012u) (CFV, 2012v) (CFV, 2012w) (CFV, 2012x) (CFV, 2012y) (CFV, 2012z) (CFV, 2012aa) (CFV, 2012ab) (CFV, 2012ac) (CFV, 2011p) (CFV, 2011w) (CFV, 2011x) (CFV, 2011o) (CFV, 2011r) (CFV, 2011q) (CFV, 2011v) (CFV, 2011u) (CFV, 2011t) (CFV, 2011s) (CFV, 2010e) (CFV, 2010l) (CFV, 2010m) (CFV, 2010d) (CFV, 2010n) (CFV, 2010g) (CFV, 2010f) (CFV, 2010k) (CFV, 2010j) (CFV, 2010i) (CFV, 2010h) (CFV, 2009j) (CFV, 2009e) (CFV, 2009l) (CFV, 2009m) (CFV, 2009d) (CFV, 2009c) (CFV, 2009g) (CFV, 2009f) (CFV, 2009k) (CFV, 2009i) (CFV, 2009h)

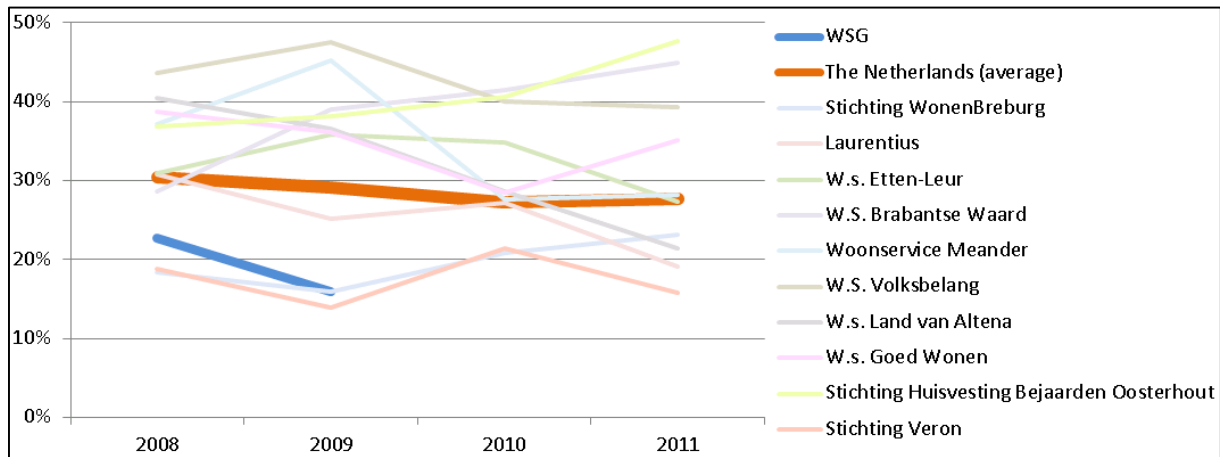


Figure XII.4: WSG social capital 2008-2011 compared

### Corporation profile

Achieving growth on the short term is relatively hard for a corporation, considering the long lifetimes of equity. As the overall corporation equity remain nominally equal, with a growing total account balance, the buffering capacity will lower (in Dutch, these are called 'verduunningseffecten'). Also, WSG was only limited depreciating on its tangible fixed assets under development. This caused WSG to be selected by CFV for further research every year in the period 2001-2011.

In 2010, it became clear to CFV that WSG had more ground positions than it reported and that these positions also had more obligations than reported. It proved this happened more because of the limited insight in the internal organization than it was fraud. At the times of the request of financial restructuring support, WSG had over 500 m<sup>2</sup> of ground position for each housing unit it operated at the time (CFV, 2010n).

Eventually, the WSG obligations resulted in liquidity shortages. In October 2012 it was decided that autonomous existence of WSG was no longer possible and that CFV would provide an interest free loan of €21 million in order to remain some buffering capacity while selling to property to surrounding corporations (CFV, 2012ae).



## Appendix XIII – Creativities to engage in risk taking

For peers to be able to monitor each other's risk taking, fairly deep insight in the investment decisions is required. Note the ways a corporation can engage in risk a practically infinite. Hence, the aim of this appendix is not to discuss all options for corporations to engage in risk. This appendix gives notion to creativity used to engage in risk taking and the challenges this brings for monitoring corporation behavior. For this reason, this appendix discusses three examples. First, the strategy of (Dutch:) 'slepen' is discussed. Second the use of subsidiaries (Dutch: 'dochterondernemingen') is elaborated upon. The third example discusses a trick to use disinvestments in social capital for commercial activities.

### 'Slepen'

Since 2007, WSW guarantees corporation loans through so-called facilitation volumes. The facilitation volume is the amount of loans WSW is willing to guarantee for a corporation (for a maximum of three years) in advance. Like any WSW guaranteed loan, these financial means may only be utilized for DAEB purposes.

However, in the DAEB services it is included that loans may be utilized to temporarily help maintain a sufficient liquidity position. In the grey area of this arrangement, corporations can still use (the cheap) WSW guaranteed money for participating in non-DAEB projects. Only precondition is that this financing is temporarily. For example, this enables corporations to use their facilitation volumes to finance the development of build housing when not sufficient property is sold yet. In the sector, this is called 'slepen'. Risk is that developed property will not be sold at all (or for lower prices), thereby making the 'temporary' financing 'definitive'. For regulators, especially peers, 'slepen' is hard to regulate on as it 1) is not illegal, and 2) requires deep insight in corporation cash flows and cash allocations.

### Subsidiaries

Since 2008, corporations are bound to the partial corporate tax (Dutch: 'partiële vennootschapsbelasting'). In this light, agreements were made between the Dutch Tax Authority and the sector on manage parts of the equity through the Dutch legal entity form of B.V. Amongst others, this included the commercial, expensive rent, and planned demolition equity (this is named 'VSO equity' in figure XX.1). Simultaneously, (some) corporations were busy in utilizing their social housing equity for commercial purposes better.

Corporations were now able to set up a B.V., they are full owner of. This creates the opportunity to 'create' money that may be used for commercial purposes. This requires three steps, also shown in figure XX.1. First, the corporation pays of any of the remaining loans on the equity. In practice, these loans are not physically paid off, but spread over the equity that will remain in the corporation. Hence, the loan on the future B.V. equity is kept within the corporation.

Second, the B.V. buys the 'VSO equity' from the corporation. This makes that the equity now is free from DAEB regulation as it is no longer directly connected to WSW loans or social capital of the corporation. In figure XIII.1, this is referred to as 'B.V. equity'. In fact, the corporation provides a loan to the B.V. to make it capable to buy the equity. However, this loan is not directly linked to DAEB regulation.

So now there are two organization with two different pools of equity, whereof the B.V. equity is 'free' possession. The B.V. may now attract extra financial loans on its equity. This comprises the third step. The B.V. equity, based on market values, is already financed for a big part through the corporation loan. However, banks will be willing to invest in the B.V. as long as their loan conditions outrank the conditions of the loan provided by the corporation. This way, the B.V might enlarge its equity position. The commercial capital can now be used to engage in commercial activities. Factually, the B.V. is over financed. However, the risk (i.e. the loan value no longer covered by pledge) is fully for the corporation. Still, no single illegal action has taken place. Also, this trick can be repeated over sub-subsidiaries to further cover financing activities, making it a pyramid game.

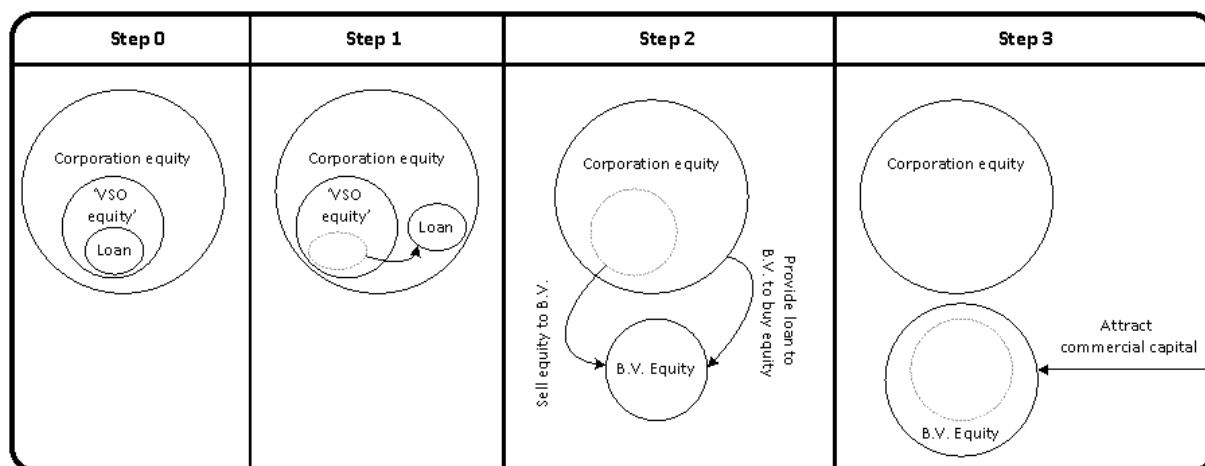


Figure XIII.1: Capital 'creation' using subsidiaries

Also in this case, monitoring is hard as this value creation mainly concerns internal transactions and steps. Also, subsidiaries may serve other purposes that are less risky. Regulating on this organizational variation and corresponding financing decisions requires very deep insight in financial details and contractual terms. Still, as the B.V. is owned by the corporation, elements are visible on the corporation balance sheet. The use of subsidiaries is one of the elements that provided Servatius with the financial means to engage in the Campus project.

### Usage of social capital disinvestments for commercial activities

A discrepancy in WSW regulation still makes it possible for corporations to use their social capital for commercial purposes. When a corporation plans to engage in a new project in the public domain, it will approach WSW for a guaranteed loan. Suppose the corporations claims to need an investment of €100 million. WSW is willing to guarantee a loan of €50 million, the other €50 million is gathered by the corporation through disinvestment (e.g. selling of) current social capital. This is all ok and legit. Now, maybe the corporation only invests €80 million. The corporation will claim it used the €50 million of WSW guaranteed loans, and €30 million of the disinvested capital. The remainder €20 million can now be used for other purposes, like commercial activities. Strictly speaking, this should not be possible. However, preventing this situation requires monitoring on the project level. The WSW judgment up front is not aligned to the monitoring at the back. Especially active corporations know and utilized this weakness in regulation.