Uttlesford District Council
Briefing on the HRA Business Plan Modelling

1. Introduction

1.1 ConsultCIH have been assisting the Council with developing an HRA Business Plan to identify the future financial position for the authorities housing stock.

1.2 The Government issued on the 1st February its proposals to reform the HRA with the withdrawal of the housing subsidy system which builds upon previous rounds of consultation for HRA reform. It forms part of the Localism Bill which should receive royal accent in the autumn securing the reform of the HRA from April 2012.

1.3 This briefing seeks to identify the financial position under both scenarios for pure comparison though it should be acknowledged that self-financing will be introduced in April 2012.

1.4 This briefing also considers the next steps the Council should consider in preparing for self-financing.

2. Uttlesford's modelling: main assumptions

2.1 An HRA business plan model has been produced for Uttlesford launched from 2011/12 and based on the existing budget, with the following key assumptions:

- Balanced to the 2011/12 HRA budget and 2011/12 capital programme with the exception of a revised reduction in supporting people grant
- Rents converge (with similar housing provider properties) in 2015/16 (with no property-by-property adjustment for caps and limits[1])
- General Inflation (RPI) set at 2.5%
- Roll forward of management and maintenance expenditure with inflation
- Roll forward of non-rent income with inflation with the exception of supporting people grant
- Right to Buy sales of 6 per annum
- New build of 5 properties and 18 demolitions

2.2 A critical assumption relates to the stock investment and capital needs for the stock over the longer term. These have been factored into the business plan based on the Michael Dyson Associates survey of August 2009. The 30 year capital profile inflated to 2011 prices amounts to around £34.5k/unit

[1] Caps and Limits refer to restrictions on individual rent increases of RPI plus 0.5% plus 2% and not breaching a set rent (for housing benefit purposes) for a property, dependant on the number of bedrooms

ConsultCIH Ltd
4 Riley Court,
Millburn Hill Road,
Coventry, CV4 7HP

www.consultcih.co.uk
EMail headoffice@consultcih.co.uk
Telephone 024 7647 2720
Registered in England and Wales: 01754648

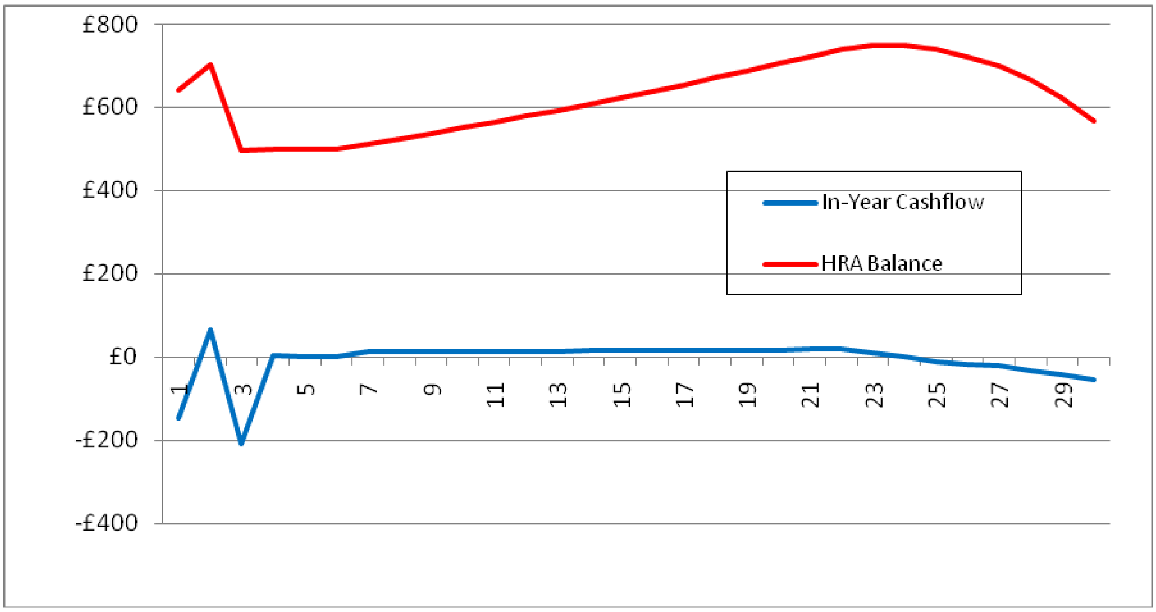
(excluding fees) and this is in line with benchmarks, as would be expected from the survey process that has been undertaken.

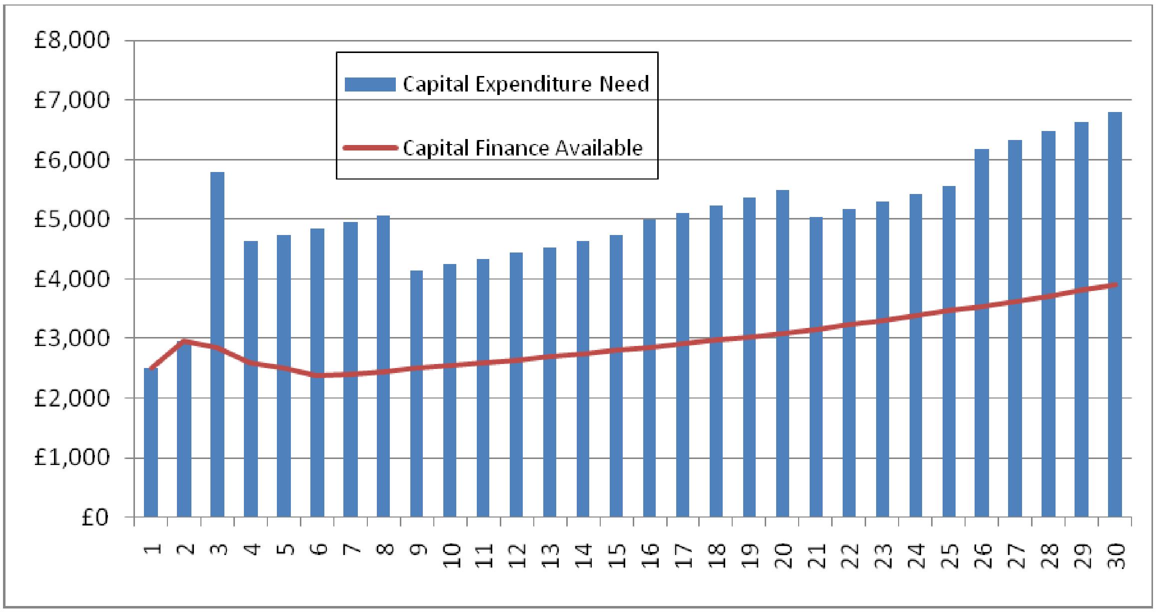
2.3 The stock condition survey identifies that in 2013.14 a significant level of expenditure is required and we have re-profiled £5m of this between the preceding year and five following years.

3. Summary Outcomes for Remaining in the HRA Subsidy System

3.1 As stated previously we have modelled the position if the subsidy system was to remain and this is demonstrated in the charts 3a and 3b below:

Charts 3a and 3b: Revenue and capital profiles remaining in the subsidy system £'000





ConsultCIH Ltd
4 Riley Court,
Millburn Hill Road,
Coventry, CV4 7HP

www.consultcih.co.uk
EMail headoffice@consultcih.co.uk
Telephone 024 7647 2720
Registered in England and Wales: 01754648

3.2 The above chart 3a demonstrates that the HRA remains in a balanced position over the 30 year period.

3.3 Chart 3b however demonstrates that if the subsidy system were to continue that the capital investment required, as identified by the stock condition survey, could not fully funded beyond year 2. The cumulative shortfall, including inflation, would be in the region of £88m over the 30 years.

4. Comparing self financing (HRA Reform) to subsidy

4.1 Self financing HRA business plans on the basis of the current proposals are almost universally better funded than plans based on an unreformed subsidy system. This is the case for Uttlesford and principally arises as a result of the following key factors:

- The benefits of all net rent increases are available to the plan – i.e. surpluses are not captured nationally and redistributed; this is the critical difference between the two futures as rental surpluses are expected to be rise sharply in the future.
- The allocation of uplifts for M&M and major repairs allowances gives additional spending power from day one.
- The interest charge on debt is at a rate lower than the discount factor used in the settlement calculation.
- The opening debt is lower than that identified in the settlement (due to the difference between the CFR measures).

5. Proposed settlement for Uttlesford

5.1 The headline debt settlement from CLG for Uttlesford amounts to £86.661m. This is based on uplifted subsidy allowances of 15.26%.

5.2 The settlement has also made provision for debt management expenses and an allowance of £59 per property per year for disabled adaptations included in the above uplift to allowances.

5.3 Another amendment to the original proposals is the inclusion of an assumed level of right to buys at an average of 5.7 per year. This reduces the debt settlement by approximately £1.97m. However the continuation of the 75% of pooling of right to buy receipts has been confirmed for the next 4 years within the comprehensive spending review and is likely to continue on the basis of the reduction of the debt settlement. The un-pooled 25% can continue to be spent on either general fund or HRA investment.

5.4 Given a settlement of £86.661m, the debt adjustment for Uttlesford is £88.155m which is arrived at by offsetting the existing HRA 'notional' debt SubsidyCFR[2] of £0.476m. This results in an 'opening self financing debt at

[2] The HRACFR is the actual element of the council's overall surplus or debt relating specifically to Housing. The SubsidyCFR is the assumed level of surplus or debt within the current subsidy system for the council's HRA.

ConsultCIH Ltd
4 Riley Court,
Millburn Hill Road,
Coventry, CV4 7HP

www.consultcih.co.uk
EMail headoffice@consultcih.co.uk
Telephone 024 7647 2720
Registered in England and Wales: 01754648

1/4/2011' of £85.882m when taking into account the HRA has no debts and has capital reserves of £0.303m. The existing differential between subsidy-debt (Subsidy CFR) and actual reserves (HRACFR) of £0.779m is therefore retained as borrowing potential within the new system for Uttlesford.

.

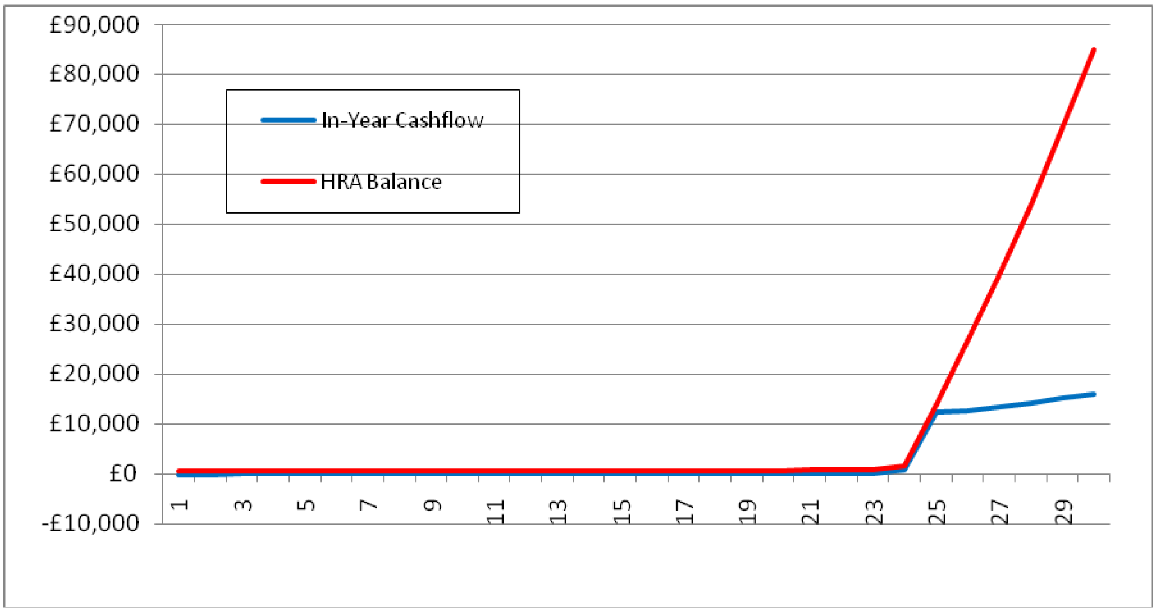
6. Headline outputs for Self-Financing (HRA Reform)

6.1 We have modelled the impact of self-financing with the following assumptions:

- Long-term interest rates of 6% (from PWLB)
- Repayment of debt whilst retaining a minimum balance on the HRA of £0.5m (inflated)
- Depreciation based on the stock condition survey in-line with the latest CIPFA consultation

6.2 The following charts demonstrate the projections for both the HRA, funding of the capital investment requirements and debt repayment:

Charts 6a and 6b: Revenue and Capital profiles remaining under self-financing £'000



ConsultCIH Ltd
4 Riley Court,
Millburn Hill Road,
Coventry, CV4 7HP

www.consultcih.co.uk
EMail headoffice@consultcih.co.uk
Telephone 024 7647 2720
Registered in England and Wales: 01754648

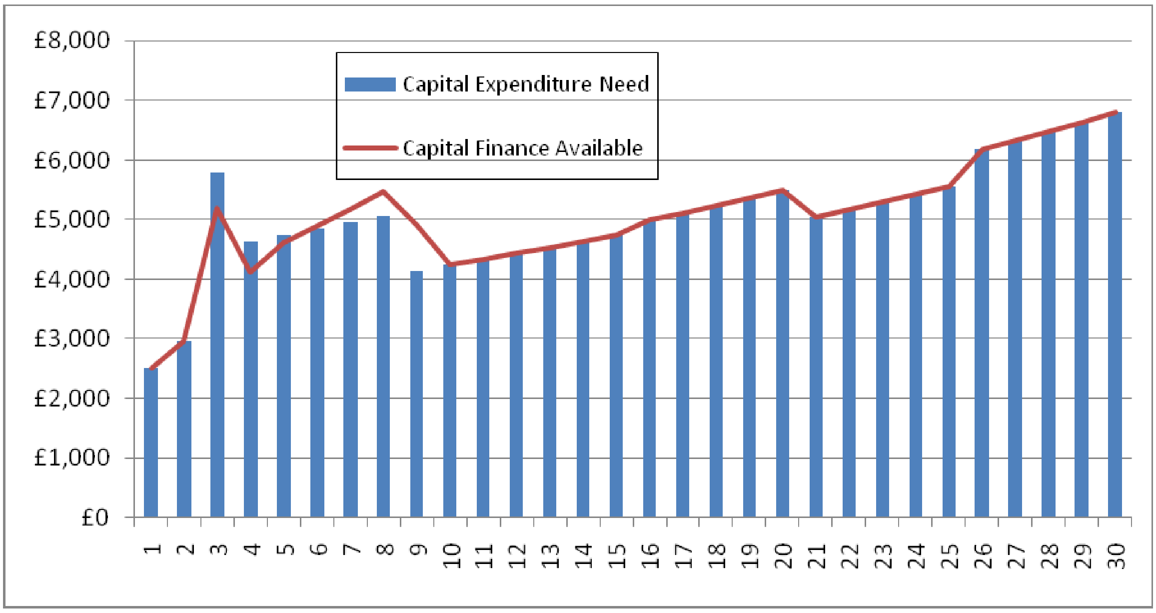
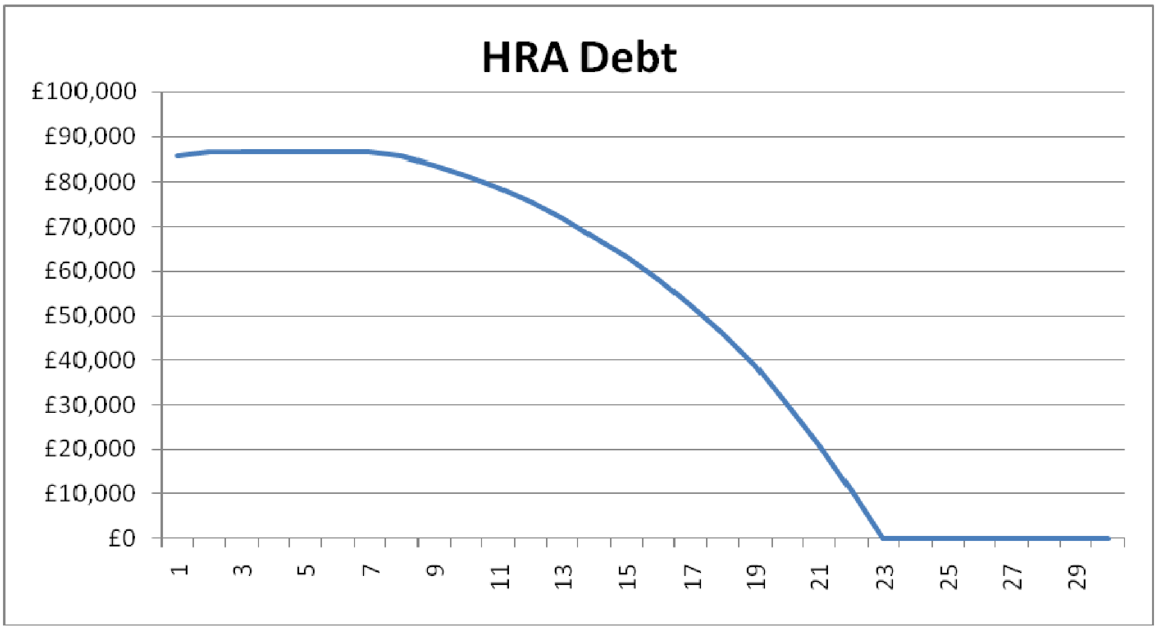


Chart 6c: Debt profile following self-financing in 2012.13 £'000



6.3 Chart 6c above demonstrates that the debt attributed can repaid as early as 23 years from take on and shows clear viability on the basis of the assumptions within the plan.

6.4 Chart 6a demonstrates that the minimum balance of £0.5m can be maintained whilst funding capital investment and debt repayment where possible with balances accumulating after year 23.

6.5 The high-level of investment required, as identified in 2.3 above, means that even with the utilisation of reserves and debt headroom there is still a shortfall initially of funding the full investment programme as shown in chart

ConsultCIH Ltd
4 Riley Court,
Millburn Hill Road,
Coventry, CV4 7HP

www.consultcih.co.uk
EMail headoffice@consultcih.co.uk
Telephone 024 7647 2720
Registered in England and Wales: 01754648

6b in years 3 and 4. However the shortfall is fully funded by year 10 of the plan.

7. Sensitivities

7.1 The plan is viable and resilient to changes in key assumptions. Some key headlines are set out below.

7.2 If interest rates were 7% not 6%, the debt repayment plan redeems debt by year 27 (compared to year 23). Overall the plan remains viable with considerable reserves at year 30.

7.3 Real inflation in capital costs (1% pa for 10 years) results with debt repayment pushed out to year 24. Overall the plan remains viable with considerable reserves at year 30.

7.4 Real inflation in management and maintenance costs (additional 1% pa for 10 years) reduces revenue surpluses but results in the plan remaining viable with considerable reserves at year 30 and debt repaid by year 25.

7.5 It should be noted that any additional expenditure above those assumed within the plan will result in the back-funding of the investment programme extending. For example as in 7.2 if the interest rate is 7% then the time to meet the backlog extends by 5 years.

8. Next Steps for Uttlesford

8.1 There are a number of technical issues which are still to be resolved at the national level. These include the treatment of depreciation and the approach to the separation of debt between the General Fund and HRA. These are being currently consulted on by CIPFA and we have made appropriate assumptions within the modelling to reflect the suggestions made within the consultation. Uttlesford may consider making a response to the consultation.

8.2 The debt cap has been clearly set, though the proposal does allow for prudential (unsupported) borrowing undertaken in 2010.11 to be taken into account therefore increasing the headroom. In addition any prudential borrowing undertaken within 2011.12 maybe allowed subject to approval by CLG. Uttlesford need to inform CLG of any prudential borrowing planned for 2011.12 and note that it will only be considered for inclusion in the debt cap for previously approved new build schemes. The borrowing should be undertaken before January 2011 and approved by CLG beforehand for inclusion in the debt cap.

8.3 In June a return will be issued to inform CLG for any property changes proposed and right to by sales to date to inform the revised debt settlement for early next year. This includes planned demolitions to which CLG will look for proof of approval through the committee process.

ConsultCIH Ltd
4 Riley Court,
Millburn Hill Road,
Coventry, CV4 7HP

www.consultcih.co.uk
EMail headoffice@consultcih.co.uk
Telephone 024 7647 2720
Registered in England and Wales: 01754648

8.4 As the council is taking debt on, there are some options in terms of Treasury Management (for example long term fixed rate loans vs variable rate loans). It should be noted that the government has expressed a desire to move to a greater GF/HRA separation of debt and the council should work through the implications carefully. It will be expected that Uttlesford will approach the PWLB with its plans as to how to fund the debt settlement through a variety of loan facilities with differing durations according to the planned expenditure.

8.5 Furthermore as the General Fund currently benefits from the average overall CFR, with the HRA taking on debt, it is expected that the Consolidated Rate of Interest (CRI[3]) credited to the General fund would not change, if there were a separation of debt. At this stage we do not see any detrimental effects to the General Fund, as it is not currently in debt.

8.6 It is anticipated that the final debt settlement figure will be produced in early January 2012.

9. Risk and reward

9.1 Moving to a self financing system significantly alters the risk profile in HRA business plans and the council housing service.

9.2 The risks of the current system focus on unpredictability and political intervention in the system (in the widest sense) and on the fact that significant revenue rental surpluses will leave Uttlesford to other parts of the country.

9.3 New risks are around increased Treasury Management, interest rate fluctuations and the fact that the council will have local responsibility for all spending (revenue and capital).

9.4 A robust risk management strategy is therefore an essential strategic document to support the asset management decisions within the business plan.

Simon Smith
ConsultCIH March 2011

[3] The CRI is the average rate of interest across the Councils debt or retained surpluses.

ConsultCIH Ltd
4 Riley Court,
Millburn Hill Road,
Coventry, CV4 7HP

www.consultcih.co.uk
EMail headoffice@consultcih.co.uk
Telephone 024 7647 2720
Registered in England and Wales: 01754648