BABERGH DISTRICT COUNCIL

From:	**Housing Panel**	**Report Number:**	**L143**
To:	**STRATEGY COMMITTEE**	**Date of Meeting:**	**9 February 2012**

COUNCIL HOUSING SELF FINANCING REFORMS - HOUSING REVENUE ACCOUNT BUSINESS PLAN

1. Purpose of Report

1.1 To approve and agree the key components of the initial Business Plan for the Housing Revenue Account (HRA) under the Government's self-financing reforms for Council Housing, which comes into effect from April 2012.

2. Recommendations

2.1 To approve the summary of the Council's initial 30- year Business Plan, which indicates potential HRA surpluses of around £100m, as set out in Appendix 1 and provides an initial basis for the management of its Housing Stock over this period.

2.2 To approve the Housing Panel's view that, based on the Business Plan forecasts of income and expenditure, that Council house rents are increased by 6% in 2012/13.

2.3 To note the likely debt settlement figure which the Council is required to pay to Communities and Local Government to implement the self-financing arrangements from April 2012 and the borrowing options, as set out in Appendix 2 (Note: an update on this will be given at the meeting).

2.4 To delegate authority to the Director of Finance to arrange the final details of the loan portfolio, based on the approved borrowing option, on the day determined by the Public Works Loan Board, based on interest rates on the 26th March.

2.5 To approve the debt split between the General Fund and the HRA set out in the Policy on Managing the HRA Debt, Section 8 of Appendix 4, which proposes the adoption of the two pool approach for splitting existing loans and allocates all of the Council's existing borrowing of £5.6m as at the 31 March 2012 to the HRA.

2.6 To note that a review of the initial Business Plan and the relevant policies/ strategies for future years which are associated with the new self-financing arrangements will be undertaken by the Joint Housing Board on an annual basis and the outcomes reported to this Committee.

2.7 To note the options for spending the additional resources that are available as the consequence of these reforms.

The Committee is asked to make the above recommendations to Full Council.

3. Financial Implications

3.1 These are set out in the report.

4. Risk Management

4.1 See Appendix 5, which also includes reference to the sensitivity analysis that has been undertaken on the HRA Business Plan forecasts.

5. Consultations

5.1 With the Tenants Forum.

6. Equality Analysis

6.1 Not required in relation to the proposals and recommendations in the report. These will be undertaken as necessary when the various policies, plans and strategies are implemented and reviewed annually.

7. Shared Service / Partnership Implications

7.1 This will form a key part of the integration and transformation journey and the work of the Joint Housing Board going forward.

7.2 Both Babergh and Mid Suffolk have worked closely on the impact of the self-financing reforms, including discussions on the rents and borrowing policy/options. Although there may be differences in the final approaches adopted on these, they will be based on a clear rationale and each Council's Business Plan.

8. Key information

8.1 The Government's reforms of funding Council Housing represents a fundamental change to the way in which Council House finances are managed. The Government has decided to end the Housing Revenue Account (HRA) subsidy system which has been in place for many years and replace it with a self-financing regime.

8.2 This will replace an unpopular and unfair system where, in the case of Babergh the first £1,500 of rent on every house we own is handed back to government. In this financial year, Babergh will be handing nearly £5.5m over to the Government – and this would have increased year on year under the current system. A key aspect of this change will involve Councils making a one off 'debt settlement' payment to the government, which for Babergh is likely to be £84m.

8.3 So, in future the HRA will save quite significant sums annually - more than the annual borrowing costs - resulting in a positive overall outcome for the Council. An initial 30 year HRA Business Plan has been produced that reflects:

- The forecast rent income that will be received, depending on the policy on rent increases and convergence (increases) in rents in accordance with the national social rent policy
- The estimated debt interest costs that are likely to arise, which will be influenced by the debt and borrowing strategy adopted
- A significant increase in capital investment of at least £1.7m a year for tenants e.g. bathrooms and kitchens and central heating
- In addition to the above, significant annual surpluses on the HRA (from 2014/15) that will be available to repay the £84m debt and for further investment in Council housing improvements or building new houses.

8.4 The new arrangements give control over the finances and investment of the housing stock to Councils. The initial Business Plan will be used by the Joint Housing Board, in conjunction with the service integration plans with Mid Suffolk and the new governance arrangements which have been approved to agree a common strategic direction for the joint housing service.

8.5 Although the initial Business Plan and the HRA Budget/capital programme requires decisions to be made by the Council for 2012/13 in relation to rent and debt policy, these can and will be reviewed annually by the Joint Housing Board as part of the business and service planning cycle.

8.6 Developing medium to long-term strategies and actions to fit in with the new regime and our integration plans will be taken forward, based on the draft initial action plan that is included in the HRA Business Plan. Members are asked to note the future plans to develop, review and monitor these arrangements.

8.7 The 30 year business plan shows that the reforms are a good deal for the Council and tenants and one which, even taking into account the borrowing requirements and additional capital expenditure the Council needs to make to maintain its homes, means it could be better off by something in the region of £100m over the 30 years of the plan. See Appendix 1 and 3 (linked to differing debt repayment options) for further details. It should be noted, however, that these surpluses depend on inflation rates and other factors. A sensitivity analysis has been undertaken, which shows that surpluses could in reality be lower than this.

8.8 Over time, the HRA will repay the £84m debt but the Council will be able to 're-borrow' over the next 30 years to undertake further investment in Council Housing – up to a Government cap on future borrowing, which for Babergh has been set at £98.2m. In arriving at this figure, the government assumes that the Council's future income from its rents will be in line with national social rent policy and convergence by 2015, which would require a 7.8% rent increase in 2012/13.

8.9 Members have been kept informed about the new arrangements as the Government has put the final touches to the legislative detail. This report now describes the approvals which are required to instigate the new forms and begin to establish the plans and steps the new Joint Housing Board will need to take to keep these arrangements under review. Further information on key aspects are provided below:

The Initial HRA Business Plan

8.10 The Initial Business Plan for 2012/13 provides up to date information on the nature and condition of the Council's housing stock and is designed to demonstrate the impact of the reforms on the plans for improving and modernising its housing which the Council has always agreed with its tenants.

8.11 There is a direct correlation between the Business Plan and the financial assumptions the government used to arrive at its debt settlement figure. The new funding arrangements are key to understanding the level of investment the Council can afford and also how it will determine its priorities in future years.

8.12 The Council's Business Plan demonstrates:

- That significant additional resources will be available for investment in its housing stock.
- That the investment requirements identified in the 2011 stock condition survey can be fully funded.
- That the Settlement Loan can be funded and repaid as early as around year 20.
- That there is scope for new housebuilding, regeneration schemes e.g. Tenterpiece and enhanced service arrangements within the plan.

8.13 Appendix 1 illustrates the detailed estimated financial plans for the first five years and also the potential summary financials for the 30 year life of the plan (in five year blocks). The agreement of the final loan portfolio will affect the levels of interest payable and reserves on hand in the business plan, but will not change the four key outcomes set out above.

8.14 This is a time of significant change for both Babergh and Mid Suffolk so, whilst it is important (and a Government requirement) to prepare future plans that demonstrate the viability of the new reforms for Babergh and its tenants and make annual stock investment and rent levels/income decisions to service the Council's loans, the initial Business Plan is an initial basis for the Council to develop and review further.

8.15 Service integration and transformation opportunities will provide fresh opportunities to deliver more effective outcomes for tenants of both Councils. The new governance arrangements will also allow tenants a much greater say in strategic housing and investment/other decisions in the future.

8.16 This initial business plan will be reviewed and developed further during 2012 for consideration by the Council as part of its Service and HRA budget setting process for next year and subsequent years.

Rents

8.17 Members should already be aware that the Government expects all Councils to follow a national social rent policy for increasing its rent which assumes a convergence of rent levels of comparable homes in the social housing sector by 2015.

8.18 The new financial framework has built in a number of assumptions into its models and debt settlement for Councils to ensure the longer term viability of the HRA in particular that the level of debt can be supported throughout this period by the rents collected.

8.19 Strategy Committee, at its meeting on 12th January, endorsed a 5% increase in Council House rents for 2012/13, which is lower than the 7.8% target level which is set under the government rent formula for rent convergence by 2015 - subject to the Housing Panel considering the matter further in relation to the production of the HRA Business Plan.

8.20 Very few Councils are likely to set rents for next year below the convergence rate. Just 4 of the largest 50 Social landlords are planning to protect their tenants from the average 8% rent increase nationally. The Housing Panel have considered the matter very carefully and that a higher rent increase would result in more financial hardship for those tenants who do not receive housing benefit (around 30% of tenants).

8.21 On the other hand, a higher rent increase of 7.8% would generate £1.2m additional rent income in the early years of the Business Plan, which could enable regeneration and new build schemes (subject to land availability) to start earlier than if a 5% rent increase is applied. With a 5% increase, surpluses on the HRA do not start until 2014/15 (estimated at £1.3m from that year – see Appendix 2).

8.22 Also, a lower rent increase next year will mean a higher increase in 2013/14 and 2014/15 to ensure rent convergence by 2015, which the Housing Panel agree should be the Council's policy.

8.23 Conversely, funding for regeneration schemes such as Tenterpiece could be found from the capital budget, but only be re-allocating some of the increased stock condition survey money.

8.24 This is a difficult issue but, bearing in mind that the Government has based the Council's debt settlement on the assumption that local authorities will follow the national social rent policy, there is a case to apply the higher rent increase of 7.8% and a rent policy that applies this increase to achieve convergence by 2015.

8.25 The financial impact of opting for the national social rent policy increase of 7.8% as opposed to the 5% previously discussed at Housing Panel has been estimated at £1.2m over the financial years 2012/13, 2013/14 and 2014/15. Resources of this scale could achieve the following:

- kick start a fully funded house building programme of 10 new homes (if land available) or 7 new homes (if land needs to be bought on open market)
- complete a significant remodelling of Tenterpiece
- fund 50% of a demolition and new build scheme for Tenterpiece.

8.26 However, the Tenants Forum think that a 6% rent increase may strike the right balance and Strategy Committee could, therefore, take the view that a lower increase in 2012/13 of 6% should be applied, on the understanding that a higher increase than RPI +0.5% would then be required in the following 2 years. A 6% increase will add around £4.90 a week to the average rent.

8.27 The Panel have also considered whether new tenancies should be based on the target/convergence rent immediately. Again, there are mixed views but it has been concluded that they should not as the HRA does not need additional funding.

The Council's borrowing options

8.28 The general principles around managing the HRA debt are set out in the Treasury Management Strategy documents (see Paper L132R on today's agenda). Our Treasury Management Advisors, *Arlingclose*, have concluded that the Council has 3 main borrowing options. Appendix 2 provides further details including their impact on the availability of resources for investment, the total cost of interest payable together with the advantages and disadvantages of each scenario: A brief summary of the options is provided as follows - all are on a fixed interest rate, maturity basis from the PWLB:

- Option 1 – Range of loans with staggered and regular repayment dates between years 12 and 23 reflecting that the HRA can afford to repay at this rate
- Option 2 - Similar to Option 1 but with bigger repayment chunks and most of the £84m being repaid in years 19/24.
- Option 3 - repayment as one lump sum in year 29.

8.29 The advantages and disadvantages of each approach are outlined in Appendix 3. A key strategic issue is that under each scenario the HRA will have significant additional resources available in the medium to long-term to invest in new or existing housing in the district whatever borrowing option is chosen. The options reflect the timing when the HRA will have the resources available to repay the debt: Option 1 makes the resources available towards the middle years of the 30 year plan, Option 2 makes them available more towards the end of the middle years and Option 3 leaves repayment until nearly at the end of the 30 years.

8.30 The Director of Finance is happy with all of the options but currently feels that, although Option 3 provides the greatest certainty, it costs more in interest over the 30 years and that Option 2 provides a better balance of repaying debt sooner. Further discussions are taking place with Mid Suffolk to arrive at a consistent approach and a final recommendation will then be made to Full Council on the 23 February.

8.31 The Government is offering a special one off loan deal with the Public Works Loan Board (PWLB). This arrangement is for one day, 26 March 2012, and is for the settlement debt only. The transaction will take place on the 28 March 2012 and councils will be reimbursed for interest costs incurred in 2011/12 via the Final Housing Subsidy Determination. A worst case interest rate of 4% has been used in the business plan but the actual loan arrangements are expected to result in lower rates than this on the day – perhaps of between 3.25% and 3.6% depending on market conditions between now and the 26 March.

8.32 A ‘two pools’ loan arrangement will operate in the future which separately identifies borrowing between the HRA and the General Fund. This reflects the CIPFA recommended principles to ring fencing the borrowing costs to the HRA and General Fund. As at the 31 March 2012, therefore, existing external borrowing of £5.6m will be attributed to the HRA and the General Fund will again be debt-free, albeit temporarily – the policy for this and managing the overall HRA debt is set out in Appendix 5.

Options for spending the additional resources

8.33 The financial benefits to the Council from the reforms are potentially considerable. However, the Council will need to decide its strategic direction in the short, medium and longer term to use this money in the way that it and tenants wish to.

8.34 The table below highlights some of the various options and the pros and cons of each.

Options	Pros	Cons
Increase investment in the current housing stock	• Direct benefit to tenants • Could increase rents to pay for specific improvements • Protects future assets	There would less to fund other priorities or repay debt
Increase the supply of new homes	• Helps to reduce pressure on service • Build new homes • Wider General Fund benefit • Maintains stock which may lost through RTB	There would be less to fund other priorities or repay debt
Enhance service provision	• Direct benefit to tenants	
Reduce/pay off the debt quickly	• Provides longer term ability to borrow for larger investment programmes ie; new build	Borrowing at a later date likely to cost more depending on interest rate movements (favourable rate provided for the settlement debt on one day only)

Options	Pros	Cons
Increase HRA balances for future use	• Mitigates risk i.e.; interest rates, impact of home sales, welfare benefit reforms	Reduces capacity to invest in visible benefits for tenants

8.35 Because these arrangements are very new and will change the approach to the way in which the Council's finances are managed and they come at a critical time where services between the two Councils are being integrated, it is not appropriate to attempt to resolve these questions now. In the short-term, the Joint Housing Board will need to carry out a detailed feasibility exercise on each of the options and make recommendations to each Council about how its new funding can and should best be utilised. This feasibility exercise will explore the various options in detail but is likely to ask itself:

- Should the Council continue to prioritise high profile but expensive works such as the redevelopment of its sheltered housing scheme, Tenterpiece, in addition to its existing plans and reduce its debt over a longer period?
- Should the focus of investment be linked to the development of new Council properties and new services throughout the 30 year terms of the Business Plan and borrow more when debt is repaid to make this possible?

8.36 The initial Business Plan is drafted and substantially complete. It will be finalised when Strategy Committee and Council have taken the necessary decisions. A copy of the proposed final version of the plan will then be circulated to all Members for comment. The plan includes a draft action plan and reference to other things that the Joint Housing Board will need to consider during 2012 and as part of the future service and budget planning process.

9. Appendices

Title	Location
1 - HRA Business Plan projections	Attached
2 - Loan Portfolio Options	Attached
3 - Advantages and Disadvantages of the borrowing options	Attached
4 - Policy on managing HRA debt	Attached
5 - Risk Management	Attached

10. Background Documents

None.

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Appendix 1 – HRA Business Plan projections

HOUSING REVENUE ACCOUNT PROJECTIONS
Babergh District Council

Year £'000	2011.12 1	2012.13 2	2013.14 3	2014.15 4	2015.16 5	2016.17 6
INCOME:						
Rental Income	**13,540**	**14,199**	**14,916**	**15,657**	**16,421**	**17,030**
Void Losses	**-293**	**-188**	**-179**	**-188**	**-197**	**-204**
Service Charges	**714**	**535**	**548**	**562**	**576**	**590**
Non-Dwelling Income	**215**	**220**	**225**	**231**	**237**	**242**
Grants & Other Income	**144**	**144**	**148**	**152**	**156**	**159**
Total Income	14,320	14,910	15,658	16,413	17,192	17,818
EXPENDITURE:						
General Management	**-1,842**	**-1,737**	**-1,780**	**-1,825**	**-1,871**	**-1,917**
Special Management	**-1,593**	**-1,511**	**-1,549**	**-1,587**	**-1,627**	**-1,668**
Other Management	**-5,541**	**-100**	**-91**	**-81**	**-83**	**-86**
Rent Rebates	**0**	**0**	**0**	**0**	**0**	**0**
Bad Debt Provision	**0**	**0**	**0**	**0**	**0**	**0**
Responsive & Cyclical Repairs	**-2,179**	**-2,266**	**-2,323**	**-2,381**	**-2,440**	**-2,501**
Total Revenue Expenditure	-11,155	-5,614	-5,743	-5,875	-6,022	-6,172
Interest Paid	**-136**	**-3,523**	**-3,529**	**-3,509**	**-3,453**	**-3,379**
Finance Administration	**-218**	**-189**	**0**	**0**	**0**	**0**
Interest Received	**11**	**7**	**10**	**15**	**15**	**15**
Depreciation	**-2,036**	**-3,459**	**-3,538**	**-3,621**	**-3,706**	**-3,794**
Net Operating Income	786	2,133	2,858	3,423	4,026	4,489
APPROPRIATIONS:						
FRS 17 /Other HRA Reserve Adj	**-187**	**-187**	**-191**	**-196**	**-201**	**-206**
Revenue Provision (HRACFR)	**0**	**0**	**-56**	**-1,307**	**-1,857**	**-2,236**
Revenue Contribution to Capital	**-1,198**	**-1,761**	**-2,632**	**-1,912**	**-1,965**	**-2,019**
Total Appropriations	-1,384	-1,947	-2,880	-3,415	-4,023	-4,462
ANNUAL CASHFLOW	-598	186	-21	8	3	27
Opening Balance	**1,424**	**825**	**1,011**	**990**	**998**	**1,001**
Closing Balance	825	1,011	990	998	1,001	1,028

HOUSING REVENUE ACCOUNT PROJECTIONS
Babergh District Council

Year	2011.16	2016.21	2021.26	2026.31	2031.36	2036.41	Total
£'000	1	2	3	4	5	6	
INCOME:							
Rental Income	74,733	90,425	104,195	119,913	137,993	158,788	686,047
Void Losses	-1,045	-1,085	-1,250	-1,439	-1,656	-1,905	-8,381
Service Charges	2,934	3,103	3,511	3,972	4,494	5,085	23,099
Non-Dwelling Income	1,127	1,274	1,442	1,631	1,845	2,088	9,407
Grants & Other Income	744	838	948	1,072	1,213	1,373	6,188
Total Income	**78,493**	**94,555**	**108,845**	**125,150**	**143,890**	**165,428**	**716,360**
EXPENDITURE:	0	0	0	0	0	0	0
General Management	-9,055	-10,078	-11,403	-12,901	-14,596	-16,515	-74,549
Special Management	-7,867	-8,767	-9,919	-11,222	-12,697	-14,365	-64,837
Other Management	-5,897	-450	-509	-576	-651	-737	-8,819
Rent Rebates	0	0	0	0	0	0	0
Bad Debt Provision	0	0	0	0	0	0	0
Responsive & Cyclical Repairs	-11,589	-13,148	-14,875	-16,830	-19,042	-21,544	-97,027
Total Revenue Expenditure	**-34,408**	**-32,442**	**-36,705**	**-41,529**	**-46,986**	**-53,160**	**-245,232**
Interest Paid	-14,150	-15,647	-10,748	-3,462	17	17	-43,973
Finance Administration	-407	0	0	0	0	0	-407
Interest Received	58	80	90	108	2,163	7,263	9,762
Depreciation	-16,360	-19,881	-22,331	-25,081	-28,169	-31,635	-143,457
Net Operating Income	**13,226**	**26,665**	**39,150**	**55,186**	**70,914**	**87,912**	**293,054**
APPROPRIATIONS:	0	0	0	0	0	0	0
FRS 17 /Other HRA Reserve Adj	-961	-1,083	-1,225	-1,386	-1,568	-1,774	-7,997
Revenue Provision (HRACFR)	-3,220	-17,446	-33,293	-35,690	0	0	-89,649
Revenue Contribution to Capital	-9,467	-7,997	-4,478	-17,159	-11,284	-8,645	-59,030
Total Appropriations	**-13,649**	**-26,526**	**-38,995**	**-54,234**	**-12,852**	**-10,419**	**-156,676**
ANNUAL CASHFLOW	**-423**	**139**	**155**	**952**	**58,061**	**77,493**	**136,378**
Opening Balance	1,424	1,001	1,140	1,295	2,247	60,309	1,424
Closing Balance	**1,001**	**1,140**	**1,295**	**2,247**	**60,309**	**137,802**	**137,802**

Appendix 2 – Loan Portfolio Options

Options/Scenarios

Three options/scenarios have been modelled:

Option 1 - Short Maturity – models the impact of repaying loans regularly over a relatively short period.

Option 2 - Mid Range Maturity – models the impact of largely repaying loans somewhat later and in bigger chunks.

Option 3 - Longer Maturity – models the impact of repaying the loan in the penultimate year of the business plan.

Loan Portfolio

The table below identifies the possible loan portfolio for each of the three scenarios together with the total interest payable over the period of the loans.

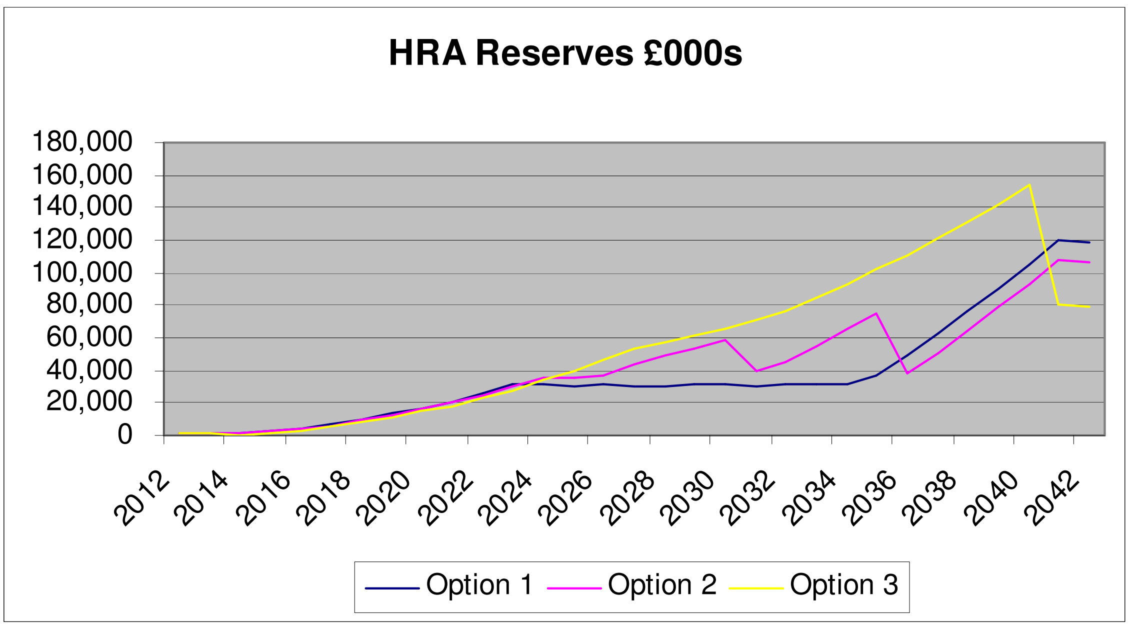
Repayment Year	**Option 1**	**Option 2**	**Option 3**
	£000s	£000s	£000s
2023/24 (yr 12)	6,000		
2024/25	7,000	6,000	
2025/26	7,000	6,000	
2026/27	8,000		
2027/28	5,000		
2028/29	5,000		
2029/30	6,000		
2030/31	7,000	25,000	
2031/32	7,000		
2032/33	10,000		
2033/34	11,000		
2034/35 (yr. 23)	4,998		
2035/36 (yr. 24)		46,998	
2040/41 (yr. 29)			83,998
Total (£000s)	83,998	83,998	83,998
Total Interest Cost (£000s)	**49,966**	**61,273**	**88,668**

Reserves Availability

The table below identifies the level of year end reserves available at five year intervals. These indicate the potential level of investment which can be made in new social housing or for reinvestment in housing stock.

Year	Option 1	Option 2	Option 3
£000s			
2017	6,701	6,136	5,300
2022	23,345	24,215	22,547
2027	30,416	44,098	53,043
2032	30,700	45,428	75,835
2037	62,352	51,045	120,936
2042	117,968	106,661	79,266

Reserves availability over the 30 year life of the business plan is shown graphically below:



Appendix 3 - Advantages and Disadvantages of the borrowing options

The advantages and disadvantages of each scenario are shown below:

Option 1

Advantages

- This scenario has the lowest interest cost of the three.
- This scenario gives the highest level of reserves by the end of the plan period.
- This scenario reduces the risks of holding high levels of cash.

Disadvantages

- This scenario reduces the amount of investment potential in the middle years of the plan.
- Any investment (beyond the capacity of the scenario) would have to be undertaken using loans that would probably be at a higher rate of interest.

Option 2

Advantages

- This scenario balances the risks and advantages of the other two scenarios.

Disadvantages

- This scenario balances the risks and disadvantages of the other two scenarios.

Option 3

Advantages

- Gives the highest level of investment potential in the early years.

Disadvantages

- Has the highest interest cost of the three scenarios.
- Could result in more cash being held than is required, and therefore interest being incurred unnecessarily.
- Could give rise to the risks associated with placing money with third parties ("counterparty risk").

Appendix 4 – Policy on managing HRA debt

1. The Government has signalled its intention not to impose a single solution for splitting current borrowing between the General Fund and the Housing Revenue Account.

2. It is accepted that HRA funds are not third party funds but funds of the Council and so will not necessarily be separately identifiable. However, local authorities should have a clear agreed policy approved by full Council for attributing income and expenditure and risks between the General Fund and the HRA.

3. The principles upon which the allocation of loans between the HRA and the General Fund should be based are as follows:

    - The underlying principle for the splitting of loans, at transition, must be that of no detriment to the General Fund
    - Local authorities are required to deliver a solution that is broadly equitable between the HRA and the General Fund
    - Future changes to the HRA in relation to borrowing are not influenced by General Fund decisions, giving a greater degree of independence, certainty and control
    - Uninvested balance sheet resources, which allow borrowing to be below the CFR, are properly identified between General Fund and HRA.

4. It is expected that, generally, only long-term loans will be split.

5. It may at times be mutually beneficial to move existing loans from the HRA to the General Fund portfolio or vice versa, recognising an appropriate 'internal' premium or discount. This avoids physically repaying and re-borrowing, which may incur significant debt rescheduling costs, particularly with the PWLB.

6. There are a number of options for the Council to consider including the adoption of a one-pool or a two-pool approach.

    - The one pool approach involves having a single pool of debt for current and new debt (pre and post settlement borrowing) and would be adopted if interest rates were not materially different (for pre and post settlement borrowing). A single pool enables the Council to manage treasury risk for the Council as a whole.
    - The one-pool approach maintains the current arrangement for apportioning costs but may restrict the Council's ability to manage interest rates over time according to the HRA's loan and risk profile.
    - If a one pool approach is approved, the Council needs to choose and evidence a fair rate of interest to charge
    - The two pool approach involves splitting existing loans between the HR and the General Fund, then allocating new loans to each pool as required. This would be adopted for clarity and transparency. Current borrowing up to the limit of the HRA Capital Financing Requirement (CFR) would be transferred to the HRA. Treasury management decisions on the structure and timing of borrowing would be made

independently for the GF and the HRA and interest on loans calculated in accordance with proper accounting practices.

- The two pool approach is favoured by CIPFA. Under the existing arrangements for apportioning interest costs, the majority of the Council's debt costs are charged to the HRA and current borrowing is less than the HR CFR. It is proposed, therefore, that the two pool approach is most suitable for Babergh and that all current borrowing be transferred to the HRA.

7. As settlement takes place on the 28 March 2012, the CFR and debt figures will not be finalised until the accounts are closed for the financial year. The proposed approach is as follows:

- The Budget and Treasury Management Strategies are to be compiled based on estimates
- Officers continue to work with the Council' treasury advisors to determine the most appropriate debt split and update this section when more detailed information is available
- The Policy on Managing the HRA debt will be included in the Strategy documents reported to Council on 23 February 2012

8. Officers have carefully considered the options in conjunction with the Council's treasury management advisors and the following is proposed:

- A two pool approach will be adopted which follows the CIPFA recommendation of maintaining two separate loan portfolios. This reinforces the ring fencing of the HRA by charging the HRA and the General Fund separately for interest costs related to the separate loan pools.
- Therefore, current borrowing of approximately ££5.6m (estimated as at 31 March 2012) will be transferred to the HRA as this is less than the HRA CFR of £6.2m. The General Fund will commence 2012/13 debt free.
- All loans will be taken from the Public Works Loan Board (PWLB) – as the PWLB are offering special rates at approximately 0.8% below current rates which cannot be matched elsewhere in the market.
- A Number of loan options are under consideration for funding the settlement debt of £84m. These options provide sufficient resources within the business plan to fund the capital programme determined by the Stock Condition Survey and allow options for future investment, such as additional investment in housing stock, regeneration and new build, lower rent increases and the provision of additional services.

Appendix 5 – Risk Management

This appendix identifies risks in the HRA business plan, together with some of the sensitivity tests which have been made to help determine their significance.

The key risks identified have been listed in the table below together with an initial assessment of their potential impact and the measures which will be taken to mitigate them.

Risk	Impact	Mitigation
Government policy	May make demands on reserves. Introduction of new requirements adds new costs. National social rent policy changes unfavourably.	Reserves utilisation policy by April 2013.
Welfare reforms	Direct payment of housing benefit to tenants increases arrears. Capping of benefits increases arrears and voids. .	Re-profile capital programme. Extend debt repayment period.
Supporting People	Further reduction in funding availability Negative impact on clients living in sheltered housing.	Older People Strategy by March 2013.
Sudden shock (financial)	Sudden costs not anticipated in HRA Business Plan.	HRA reserve of £1m. Re-profile capital programme.
Inflation	Excessive rent increases for tenants. Some HRA costs may increase above RPI.	Re-profile capital programme. Extend debt repayment period. Effective procurement practices in place.
Interest Rates	Settlement loan interest rates only known on day of loan application. Increased cost of borrowing if rates increase.	Government committed to affordable settlement loans. Settlement loans arranged at fixed rates.
Housing Sales	Loss of stock may not lead to compensating savings in service delivery. Sales proceeds not sufficient for property replacement.	Constant review to ensure efficient use of resources. Benchmarking with other social housing providers.
Specific Cost Escalation	Costs of specific items exceeds significantly beyond RPI and Babergh unable to fully recover increase. (e.g. energy costs, capital programme)	Re-profiling of capital programme. Pro-active procurement practices.
Risk Transfer	End of subsidy system transfers risks from Government to Babergh	Ongoing budgetary management. Refocus on housing strategy through annual HRA Business Planning cycle.

It should be noted that there are also a range of "business as usual" processes which help to mitigate risks on an ongoing basis.

Sensitivity analysis is a tool often used in business planning. The tool takes a base position and tests how sensitive the plan is to a change in a key assumption. The key assumptions in the base position in the Business Plan are as follows:

RPI – 2.5%
Interest rates – 4%
Capital Programme increases by RPI
Rents increased by RPI + 0.5% (after convergence is reached)
Right to Buy sales – 5 per year

Sensitivity	Yr 30 HRA Balance £m	("Cost") / Benefit to HRA £m	Debt Repayment Year
Base Position	137.8	-	20
1% increase in RPI	192.4	54.6	18
1% reduction in RPI	91.2	(46.6)	22
1% increase in interest rates	114.0	(23.8)	22
1% annual increase in capital prog	101.0	(36.8)	22
2.5% annual increase in capital prog	19.6	(118.2)	28
100% increase in voids	126.8	(11)	21
Rents increased only by RPI*	89.4	(48.4)	22
100% increase in Right to Buy sales	118.1	(19.7)	21

* Compared to RPI +0.5%

The modelling shows that the plan holds up well to the range of sensitivities which have been tested. In reality, the most likely changes will be a combination of the above sensitivities for a number of years rather than the whole life of the plan, for instance a 0.5% reduction in RPI for ten years and a 50% increase in Right to Buy sales for five years.

The business plan model will be reviewed annually and new and changing risks identified.

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