HRA Business Plan Model – "Baseline"

1.0 Introduction

1.1 The Housing Revenue Account Business Plan Model ("BPM") is the financial reflection of the HRA Business Plan ("BP"). It sets out the financial implications of the BP over a 30-year period, showing the changes year-on-year of the content of the BP. This iteration of the BP and BPM covers the years 2020/21 to 2049/50, the "BP period".

1.2 The BPM originates from HRA Self-Financing, when councils "bought" themselves out of the old Housing Subsidy system and needed to demonstrate that, including the borrowing necessary to exit the subsidy system, the income and expenditure of their HRAs would enable the self-financing debt to be repaid and management & maintenance of the housing stock would be affordable in the long term.

1.3 In MKC, the model in use has been developed from one supplied by the Chartered Institute of Housing, with both in-house and external support. Significant updates to the model, and the MK-specific content, are periodically validated by external consultants.

1.4 The principle outputs of the BPM are:

- A comparison of capital expenditure against capital resources available (including reserves, receipts, and potential borrowing) which showing the profile of the spend and resources across the BP period
- A forecast of borrowing levels required to finance the planned capital expenditure. The borrowing level is expressed as the Capital Financing Requirement ("CFR") which includes both external borrowing and internal borrowing (i.e., the use of cash balances)
- A forecast of the overall HRA balance over the BP period, assuming that surpluses are applied to reduce the CFR (i.e., repay debt) and showing the net resources left in the HRA available to fund additional capital investment or improved management and services to tenants.

2.0 Content of Baseline

2.1 This iteration of the baseline BPM is draft and will be finalised after the consultation to the main HRABP and as part of finalising the draft budget in December 2020 where it will also be subject to an independent external review.

2.2 The Baseline BPM is based on current approved plans (as expressed through capital and revenue budget approvals) and unavoidable "need to spend", principally the expenditure required to reach and maintain the Decent Homes Standard for the housing stock which is based on the Asset Management Plan ("AMP") included within the BP and stock condition and component lifecycle data held on the Keystone system.

2.3 The Baseline BPM therefore includes provision for the 5-Year Investment Programme, as set out in the AMP, and for a continuation of the programme to cover the continuing need to spend on component replacement and other planned maintenance as set out in the AMP.

2.4 The Baseline BPM also includes provision for ongoing management and maintenance costs at the levels set in current revenue budgets. These costs are inflated using corporate assumptions for long-term CPI and RPI.

2.5 The baseline also includes provision for income, principally from dwelling rents which are inflated in line with government policy and the Rent Standard published by the Regulator of Social Housing.

2.6 The baseline provides for interest on debt, and a depreciation charge on the housing stock which is recycled through the Major Repairs Reserve to finance the planned capital expenditure. In line with current policy there is no Voluntary or Minimum Revenue Provision being made to repay debt and debt charges are based on the current singe treasury pool approach.

2.7 Forecast Right To Buy (RTB) sales are included in the baseline, which have the affect or reducing rent income, reducing management and maintenance expenditure, and providing capital receipts to fund capital expenditure. An element of the estimated capital receipt is used to reduce outstanding debt to reflect the future loss to the HRA of net rental income.

2.8 Capital expenditure in the Baseline BPM includes approved capital budgets for the Housing Delivery Programme (made up of acquisitions, new build developments, and regeneration schemes) creating 148 new units. New council housing provided through this programme is assumed to be part-financed from RTB One For One ("1-4-1") receipts, and as a consequence of the rent policy, to be let at LHA-level rents. New build housing replacing stock demolished as part of regeneration schemes is assumed to be let at existing social rent levels. The issues around 1-4-1 receipts are set out in section 6 of this Annex.

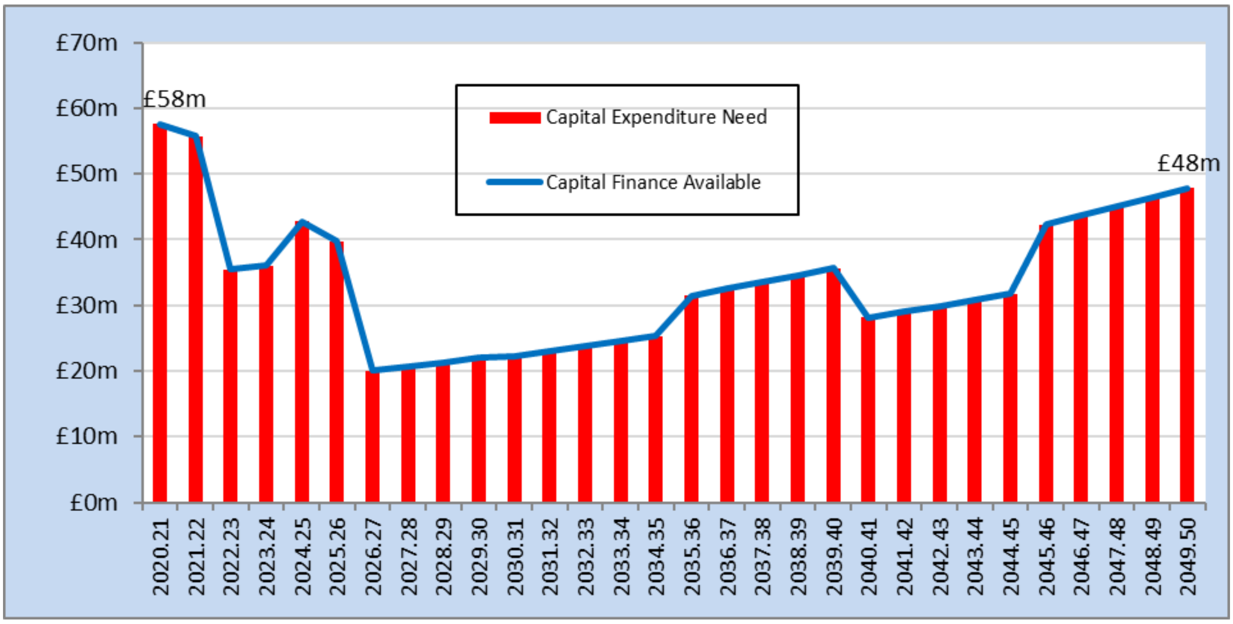
2.9 The Baseline BPM sees current housing stock of 12,071 reducing by 925 RTB sales and increasing by 148 New Builds & Acquisitions, to a total of 11,294 at the end of the BP period.

3.0 Baseline Financial Analysis

3.1 The baseline BPM is summed up in these charts, as described in para 1.4;

3.2 <u>Capital Expenditure & Resources</u>

CHART 1

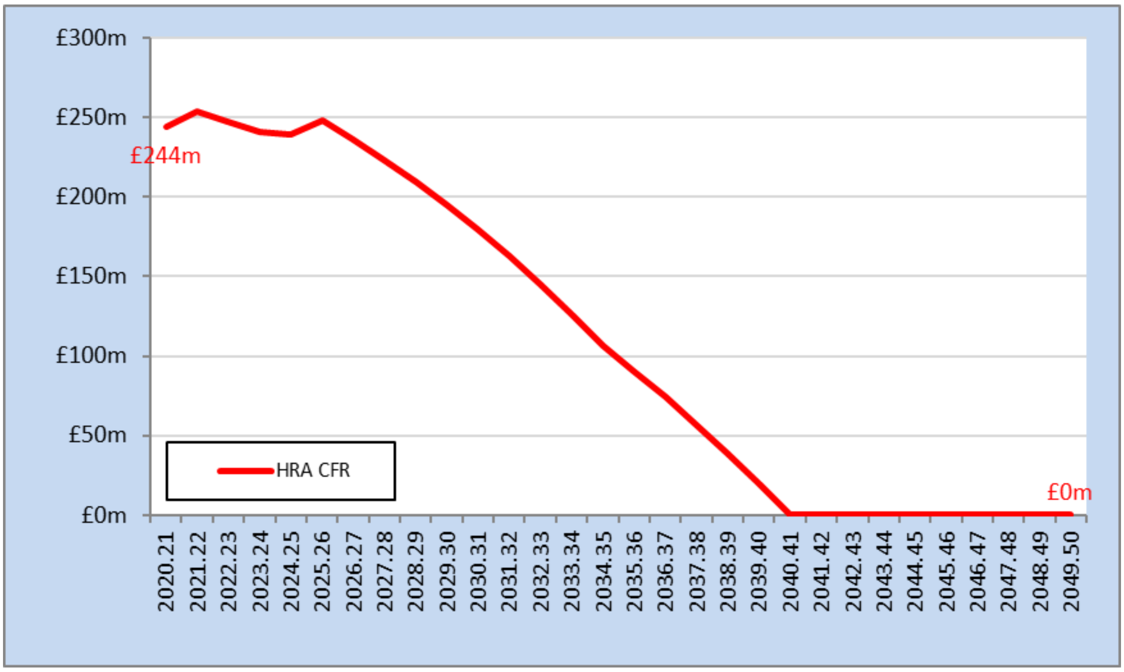


3.3 This shows the need to spend on capital that will be met from HRA resources. Peaks and troughs have been smoothed through 5-Year Investment Programmes to produce a more consistent level of spend and workload for contractors, though they will also be influenced by site-specific new build spend profiles.

3.4 The peak capital spending is £58m in a single year, though the average would be c£34m per year.

3.5 <u>HRA Borrowing</u>

CHART 2



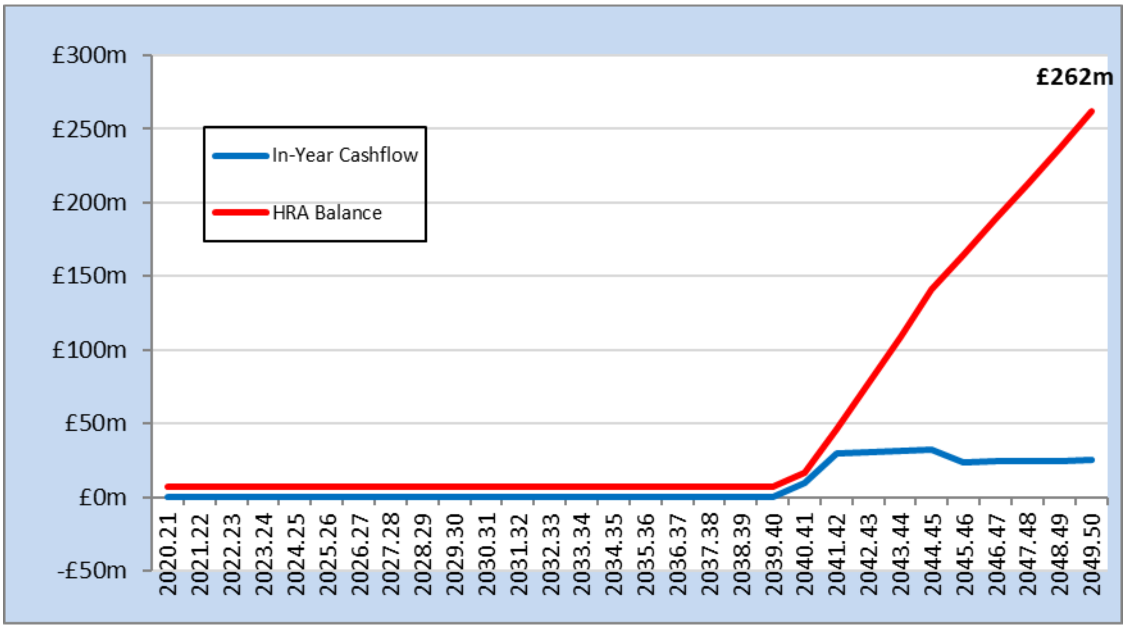
3.6 This shows that the capital expenditure required (as above) would result in a reduction in HRA borrowing requirement from the current £244m to £0m by about year 20 of the BP period.

3.7 Previous iterations of the BPM have shown that the HRA was able to repay all debt within the BP period, which is an indicator of financial viability. This modelling demonstrates that debt continues to be repayable within the period.

3.8 If debt levels were instead to be shown to increase, the HRA might be considered not to be as financially viable, and it may be necessary to review and reduce planned expenditure in order to restore financial viability. This view would be based on the ability of the HRA to generate increased net revenues that would allow it to support higher levels of debt and manage re-financing risks.

3.9 <u>HRA Balances</u>

CHART 3



3.10 This shows that the balances available in the HRA across the BP will remain at the £7m Prudent Minimum Balance (PMB) level, since all resources are being applied to finance capital expenditure, until the mid-point of the BP period.

3.11 Subsequent to that, the HRA balance increases to a total of £262m, since there are annual surpluses generated as income exceeds management and maintenance costs once interest costs have reduced to zero.

4.0 Changes from previous BPM

4.1 The BPM reported to Cabinet on 10 July 2018 showed HRA balances of £323m (with no debt outstanding) at the end of the BP period.

4.2 The change in HRA resources (balances + levels of outstanding debt) is a reduction of **£63m.** The principle changes to the BPM which have resulted in this movement are as follows:

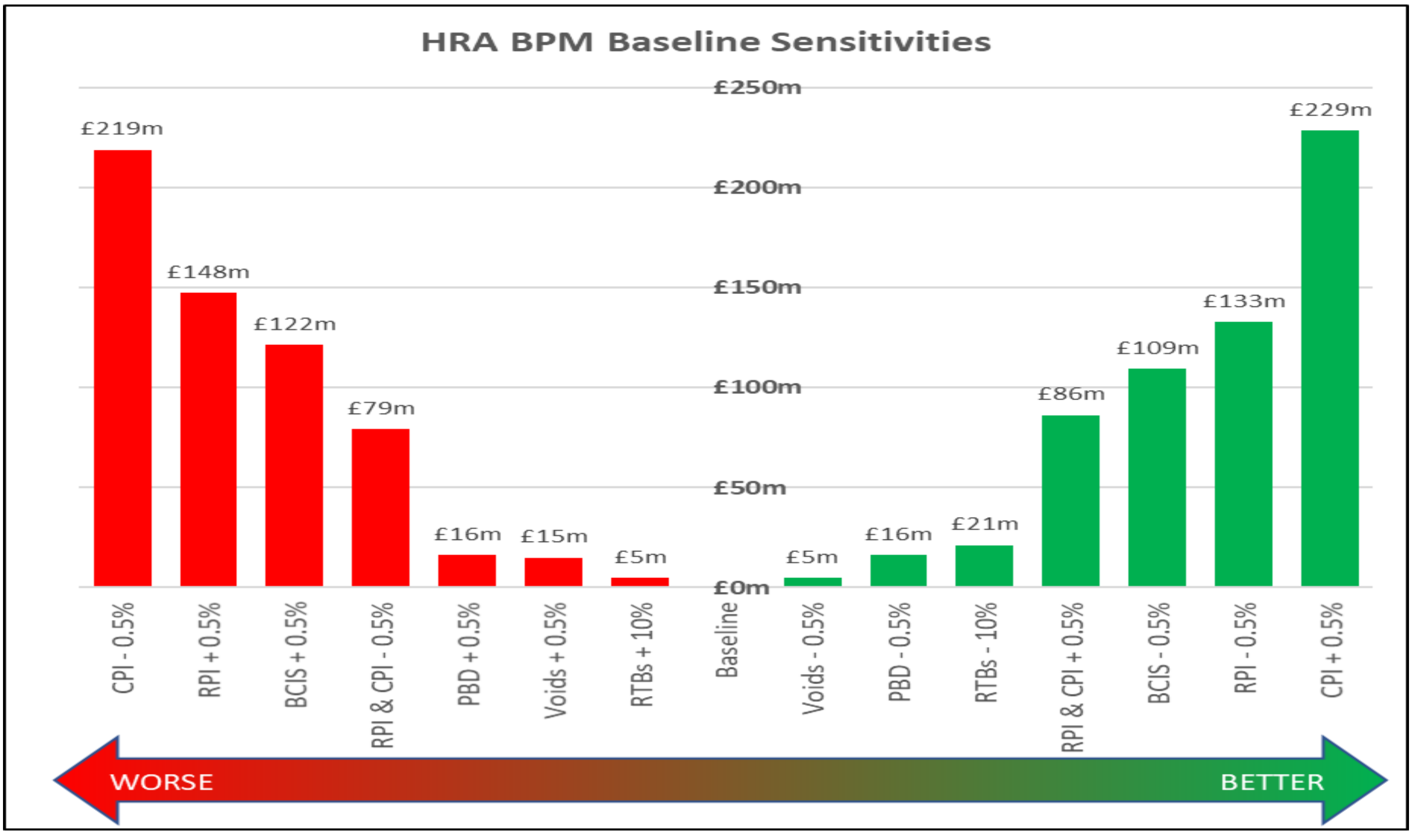
- Reduction in provision for component replacement and planned maintenance - £32m
- Reduction in provision for new build & acquisitions expenditure - £39m
- Increase in provision of 0.4% for long-term inflation on capital works - £77m
- Reduction in interest paid/earned on debit/credit balances - £6m

4.3 These figures do not exactly reconcile to the difference between the old and new BPMs because of the effects of compounding over the BP period and the cumulative impacts of these and other less significant changes.

5.0 Sensitivities

5.1 The following chart shows the range of impacts arising from a range of changes to the assumptions included within the BPM. These impacts are shown as changes in the Baseline position to the overall Revenue Balance plus HRA Debt outstanding. Impacts are not arithmetically linear as they include consequences on interest costs caused by changes in borrowing levels and other indirect consequences.

CHART 4



5.2 The chart demonstrates that the BPM is very sensitive to small changes in assumptions, with potential worse outcomes near equal to better outcomes, and so that the actual HRA will be very sensitive to small changes in the real factors modelled (and others). This indicates that the BP and BPM should be updated and reviewed periodically to ensure that changes in the outside world and the assumptions modelled are captured and used to inform planning and delivery of services and investment, maintaining sufficient headroom and flexibility to manage.

5.3 This BPM also does not reflect any refinancing risk, which is the risk that when renewal of existing borrowing or new borrowing is required, interest rates may have risen to above those modelled, resulting in increased costs to the HRA.

6.0 Use of 1-4-1 Receipts and Homes England Grant

6.1 Construction and acquisition of new council housing is assumed to be part-financed by retained 1-4-1 receipts. These receipts are required to be repaid to MHCLG, with interest, if not used for qualifying purposes. Use of these receipts also exempts the new housing from the requirement of the Rent Standard that they should be let at social rents. Our policy of charging LHA-level rents on these properties adds considerably to the value for money obtained.

6.2 Current forecasts are that spend on the Housing Delivery programme in the Baseline BPM can be 30% funded from available 1-4-1 receipts. This would not be the case if significant additions to the Programme are agreed, as would be the case in the Scenarios BPM, and the impact of this is set out in section 6 of Annex C. This would require financial assessments of individual investment proposals (acquisitions and new builds) to ensure that these are delivering both value for money relative to other options and are affordable for the HRA.