



## **HRA Acquisitions Programme**

### **Business Case**

## Outline Business Case (OBC): HRA Acquisitions Programme

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## 1. Executive Summary

This paper outlines a proposed second phase of the Housing Revenue Account (HRA) Acquisitions Programme, to build upon the successes of earlier phases, and to provide the Council and The Barnet Group with an opportunity for growth that delivers wider financial benefits for both organisations.

In November 2016 the Council approved an outline business case for the delivery of new affordable homes acquired with HRA borrowing (Phase 1). This programme saw the delivery of 21 new affordable homes for housing applicants.

Building upon this success, the Council approved various phases of purchases utilising General Fund borrowing which saw the deployment of an additional 13m budget (Phases 1 and 2) and plans to acquire an additional tranche of affordable homes outside London. By the end of Q1 2019-20, The Barnet Group will have delivered over 170 new affordable homes for Barnet's housing applicants in a little over 2 years.

	Locations	Budget	No of Units
General Fund (Phase 1)	Bedfordshire	5m	28
HRA (Phase 1)	Greater London	6.4m	21
General Fund (Phase 2)	Bedfordshire & Cambridgeshire	8m	41
General Fund (Phase 3)	Greater London	40m	106
<b>Total</b>		<b>59.4m</b>	<b>196</b>

The proposed programme will reflect learning and insights gained through the successful delivery of Phases 1, 2, and 3 and deliver:

- A robust procurement process that has been developed and refined over time
- Expertise and organisational knowledge that has been acquired through the delivery of successful programmes to date
- Scalability that affords the capacity to deliver new affordable homes in volume

The proposed programme is part of a raft of actions and mitigations introduced by The Barnet Group, in partnership with the Council to help address homelessness and General Fund temporary accommodation budget pressures. Initiatives such as the development of new affordable homes, investing in homelessness prevention activities and additional private rented sector supply through the successful let2barnet brand are key elements to the Council's approach to managing homelessness demand. The delivery of a further phase of acquisitions is another key mitigation measure that complements the range of actions undertaken and plays an important role in helping manage General Fund homelessness budget pressure.

The proposed financial model for the new programme will also generate wider benefits for both the Council and housing applicants, with funding used to acquire larger family homes within the borough, the buy-back of properties acquired under the right-to-buy programme and section 106 affordable homes in the borough.

## 2. Introduction and Strategic Context

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With a lack of affordable housing supply, high private sector rents and the impact of welfare reforms, the last few years have been a challenge for all Local Authorities with increasing homelessness demand and growing numbers in temporary accommodation which has placed pressure on already limited housing supply.

This picture has been replicated at a local level, with Barnet experiencing increased high levels of demand for affordable housing, with limited sources of affordable supply. Demand has been exacerbated by the buoyant private rental market in the borough which is increasingly unaffordable for those on lower incomes. Loss of private rental accommodation is one of the most common reasons for a homelessness application, with residents who might previously have made their own arrangements in the private rental sector approaching the local authority. To further compound matters, the Homelessness Reduction Act has generated additional demand for the borough since April 2018.

### **Supply & Demand in Barnet: A Snapshot**

- There has been a 39% increase in new Part VII homelessness applications between 2011/12 and 2017/18.
- There has been a significant increase (17%) in the number of households in temporary accommodation (numbers have increased from 2,172 in April 2012 to their current level of 2,534 at the end of January 2019).
- There was an overall 26% decrease in letting within Council stock from 2011/12 to 2017/18 and Barnet has below levels of social housing on average compared to other London boroughs.
- At the end of January 2019 there were 117 households in 4-bedroomed temporary accommodation that cost the Council approximately £190,000 per annum (before voids and bad debt) over and above rents collected

This has posed a major challenge to Barnet Homes' Housing Options Service – for example, trying to ensure that the limited supply of housing is provided to those with the greatest need, and that emergency and temporary accommodation is used effectively, whilst also attempting to identify new sources of housing supply. In addition, the cost of providing temporary accommodation has increased significantly. A key priority for Barnet Homes since 2013 has to been to strive to reduce the impact that the high cost of temporary accommodation has on the Council's General Fund (GF).

To help provide affordable housing solutions, Barnet Homes has developed and delivered a range of solutions, including developing successful cost effective long-term temporary accommodation solutions. This proposal seeks to build upon the successes and framework established in previous phases of our successful acquisition programmes to deliver a greater volume of affordable housing solutions.

### 3. Rationale

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The opportunity to acquire additional affordable housing has been revisited in line with the London Borough of Barnet's Housing Strategy and The Barnet Group's Business Plan. The removal of the HRA borrowing cap has provided Councils with the opportunity to review their HRA business plan and consider more opportunities to deliver affordable homes.

The project will involve the use of borrowing to acquire additional properties will provide the opportunity to further increase affordable housing supply relatively quickly at a lower cost than other temporary accommodation alternatives, as well as providing security of tenure to help satisfy Barnet's long-term housing needs.

This proposal supplements the previously approved HRA programme and focuses on the acquisition of a further 82 properties purchased from Q1 2019/20 onwards funded through HRA borrowing.

This approach aligns with the London Borough of Barnet's *Housing Strategy 2015-2025* that aims to:

- Increase the supply of affordable housing available to homeless households (page 27)
- Encourage institutional investment in the private rented sector (page 20)

And with the Council's Corporate Plan:

- Where services are delivered efficiently to get value for money for the taxpayer

### 4. Project Definition

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#### Project Objectives

The key objectives of this project are to:

- Increase affordable housing supply by procuring affordable homes from the open market and from affordable housing developments
- Reduce the cost of temporary accommodation and subsequent pressure on the Council's General Fund
- Increase the asset base of the borough's Housing Revenue Account

#### Project Deliverables & Outcomes

The key project deliverables are listed in the table below:

Deliverable	Details	Timeframe
Business Case (incorporating options analysis)	Undertake research analysis and identify options for acquisition of properties. Development of a business case that includes options analysis, preferred option, financial modelling, risk management etc.	December 2018 to February 2019
Presentation of	Presentation of options, and preferred approach	March 2019

Deliverable	Details	Timeframe
recommendations	to the London Borough of Barnet	
Approval	Approval (approach)	March 2019
Approval	Approval (budget)	March 2019
Implementation	Procurement of properties in accordance to the preferred approach	Q1 2019/20
Review	Review & benefits realisation	On-going

## 5. Options

Our learning and insight gained through the delivery of a successful acquisitions programme since Q3 2016/17 has proven invaluable and has helped formulate future scheme planning. The market in London has recently stabilised and our experience to date has evidenced that there is a supply of units to be acquired that can be delivered at more affordable levels than temporary accommodation alternatives.

In response to the analysis and feedback received on our existing schemes, the following approaches have been explored in more detail.

### 1. Do nothing - continue to acquire properties outside London on licence from existing temporary accommodation providers

Existing temporary accommodation rates mean that for each new household placed in 2-bed emergency temporary accommodation costs the Council approximately £2,400 net per annum. With bad debt provision and management costs factored in, this figure increases to approximately £3,400 net per annum, per household. Where properties are sourced outside London, these costs reduce significantly, however it still represents a net cost per unit of almost £1,900 per annum at current prices.

This 'do nothing' position represents a potential net present value of cash flow of (£146k) per unit over the next 40 years and would mean there is no positive financial impact to forecasted future General Fund budget pressures. Should inflation in the cost of delivering alternative temporary accommodation options increase, then this will further increase the pressure on the Council's General Fund. It is therefore not recommended.

### 2. The Council acquires assets from the open market, and affordable housing developments in Barnet, funded through Housing Revenue Account borrowing

The Barnet Group would source and deliver assets secured from the open market and purchases would be funded by the Council via PWLB borrowing at a current rate of approximately 2.8%.

Barnet Homes would provide a full management service for properties acquired and units would be used to provide secure accommodation, at 65% of the market rent. The units would be let on flexible tenancies.

The programme will be part subsidised with £1m right-to-buy receipts.

## Proposed hurdle rate

To provide TBG with flexibility with which it secures assets for the programme, it is proposed that the following conditions be set as minimum requirements for acquisitions:

1. Assets acquired must deliver a **positive NPV of cash over a 50-year period**
2. Assets acquired must be within the London Borough of Barnet

Learning from previous phases has demonstrated that the success of programmes is contingent on the level of flexibility afforded through governance. The proposed minimum requirements will enable TBG to consider a wider range of opportunities (including s106 acquisitions and bulk purchases) based upon their outputs and provide the ability to act swiftly to secure assets for the Group.

### Key benefits

There are several key benefits realised through this model:

- Delivers at a net cost of **£40k per property over a 40-year** period that is more favourable than existing methods of providing **temporary accommodation which could potentially cost £274k per unit** over a similar period.
- Delivers a significantly **better NPV** to alternative temporary accommodation options over a 40-year period (198k vs -146k) for alternative temporary accommodation).
- Would provide an almost immediate, positive impact to the Council's General Fund, through the delivery of additional affordable homes as an alternative to existing temporary accommodation.
- The model provides certainty of long-term temporary accommodation costs with future costs not subject to as yet unknown inflationary pressures.
- The model provides security of tenure to satisfy the Borough's long-term housing needs.
- The Council will be able to acquire a mixture of s106 units, ex-Council stock and a series of larger units from the open market to help meet demand for larger households.

### Treasury strategy

The proposed approach will take advantage of increased borrowing capacity within the HRA. The risk of increased borrowing is minimal as this is borrowing to fund affordable housing, recognised as a low risk investment. The risk of rising interest rates in the period before drawdown will be mitigated by a gateway review of each borrowing commitment, confirming the capacity of the model to repay the loan within 50 years.

### Suggested approach

It is recommended that the option to purchase units from the open market and affordable housing developments (option 2 is approved).

## 6. Expected Benefits

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Please refer to **Appendix A** for a summary of expected benefits for this project.

## 7. Risks

Please refer to **Appendix B** for a summary of key risks and mitigating actions.

## 8. Financial Appraisal

The project would be funded through HRA borrowing. The programme would deliver approximately 82 units of affordable homes in borough.

A breakdown of the anticipated mix of units is provided in the table below.

*Table 1 – Expected unit breakdown*

Property Size	Number of acquisitions
One Bedrooms	5
Two Bedrooms	26
Three Bedrooms	31
Four Bedrooms	20
<b>Total</b>	<b>82</b>

The tables below summarise the overall position of the models proposed, using average property purchase prices and rents expected to be delivered through the scheme<sup>1</sup>.

*Table 2 - Summary of cash flow impacts per unit*

Activity / cumulative impact	Year 1 Revenue Cost	Year 10 Revenue Cost	Year 20 Revenue Cost	Year 30 Revenue Cost	Year 40 Revenue Cost	Year 50 Revenue Cost
Existing TA	2,857	38,381	92,534	168,080	273,566	420,985
HRA purchasing	7,261	57,811	87,234	83,779	40,247	52,140
Saving	(4,404)	(19,430)	5,300	84,301	233,319	368,845

*Table 3 – Summary of impacts per unit*

	HRA purchasing
Average property price	340,610
Average delivery costs	49,592
Subsidy	12,195
Total borrowing per unit	378,007
Peak cash deficit	90,169 (Year 25)
NPV (50 years)	254,521

Where the Council were to acquire 82 units through Housing Revenue Account borrowing, the overall financial impact would likely deliver significant financial benefits.

<sup>1</sup> Figures quoted relate to prospective purchases in Barnet only.



*Table 4 – Overall scheme summary*

	HRA purchasing
Volume of units	82
Total revenue cost after 50 years	(4.28m)
TA cost avoidance over 50 years	34.5m
Capital growth over 50 years	61.3m
Total Rent Roll pa (Year 1)	1,186,842

Acquiring affordable homes through HRA borrowing delivers a significantly better net present value of cash flow than existing temporary accommodation options.

*Table 5 – Net Present Value of cash flow over 40-year period*

	NPV
Existing TA	(176,911)
HRA purchasing	254,421

### Stress-testing of the financial model

Given the length of term of the programme and arrangements that the Council would be required to commit to, stress testing the assumptions is important to gauge the financial impact where some of the assumptions are not realised. The table below indicates the potential impact per unit where some of the key assumptions vary.

*Table 6 – Stress testing financial models*

	HRA Purchasing Net Present Value	HRA Purchasing Revenue Surplus @40 years
Base Case	254,421	52,140
10% increase in average purchase price	234,107	(37,653)
10% reduction in average rent	195,573	(69,916)
1% Increase in borrowing rate	197,247	(136,863)

In summary, where there are variances in the assumptions, the model continues to realise benefits in comparison to alternative temporary accommodation options.

## 9. Dependencies

### Assumptions

- Timely provision of any requested information and input from senior stakeholders.
- On-going political support for The Barnet Group to undertake acquisitions and for the on-going management of these properties.
- Ability to implement cost effective, quality management and maintenance arrangements for the acquired properties.
- Supply of stock suitable for purchase remains available and market conditions remain favourable.

## Constraints

- There may be a lack of available supply in borough that satisfies the requirements of the programme

## Interfaces / Dependencies

- The Council and will need to approve the proposed approach, for the project objectives to be achieved
- There are other initiatives and projects underway that are also aimed at increasing affordable housing supply.

## 10. Approach to Consultation

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A range of stakeholder consultation and engagement has occurred as part of the public engagement programme developed for the London Borough of Barnet's Housing Strategy.

A summary of these activities includes:

- The Housing Strategy consultation ran for three months, from 5th November 2018 to 11th February 2019, alongside the Homelessness and Rough Sleeping Strategy consultation. It primarily consisted of an online survey on Engage Barnet. Supporting documents were also available on Engage Barnet, allowing residents to view the draft strategy on there.
- In addition, presentations were made to the Barnet Homes Performance and Advisory Group, the Children's Partnership Board, the Youth Board and Health and Well Being Board.
- A roadshow was also held in November 2018 for residents to meet the chair of the Housing Committee, and give their views on the strategy. This event had a particular focus around private renters, inviting attendees to share their experiences of residing in that sector.

## Appendix A: Benefits Realisation

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Benefit Type	Description of the benefit	Who will benefit	Expected benefit value	Financial year that the benefit will be realised	Benefit Owner	How will the benefit be measured	Baseline value (£, % etc) and date
Financial	Temporary accommodation cost avoidance	LBB	Up to £22.5m over 40 years	From Q1 2019/20	LBB	Financial monitoring	
Strategic	Increase of affordable housing stock	LBB Housing Applicants	82 units	From Q1 2019/20	LBB	Performance monitoring	
Financial	Capital growth	LBB	Up to £47.9m over 40 years	From Q1 2019/20	LBB	Financial monitoring	

## Appendix B – Financial Model

### 1. Individual unit Income and Expenditure sheet (HRA Purchasing Model)

	Year 1	Year 5	Year 10	Year 15	Year 20	Year 25	Year 30	Year 35	Year 40	Year 45	Year 50
<b>Income</b>											
Rent	14,474	16,290	17,986	19,858	21,925	24,206	26,726	29,508	32,579	35,970	39,713
<b>Gross income</b>	<b>14,474</b>	<b>16,290</b>	<b>17,986</b>	<b>19,858</b>	<b>21,925</b>	<b>24,206</b>	<b>26,726</b>	<b>29,508</b>	<b>32,579</b>	<b>35,970</b>	<b>39,713</b>
<b>Expenditure</b>											
Routine Maintenance	750	812	896	990	1,093	1,206	1,332	1,471	1,624	1,793	1,979
Management Cost	500	541	598	660	728	804	888	980	1,082	1,195	1,319
Service Charge & Ground Rent	1,200	1,299	1,434	1,583	1,748	1,930	2,131	2,353	2,598	2,868	3,167
Void Loss & Bad Debt	579	652	719	794	877	968	1,069	1,180	1,303	1,439	1,589
Interest	10,395	10,395	10,395	10,395	10,395	10,395	10,395	10,395	10,395	10,395	10,395
Major Works	750	812	896	990	1,093	1,206	1,332	1,471	1,624	1,793	1,979
MRP	7,560	7,560	7,560	7,560	7,560	7,560	7,560	7,560	7,560	7,560	7,560
<b>Net Expenditure</b>	<b>21,734</b>	<b>22,071</b>	<b>22,499</b>	<b>22,972</b>	<b>23,494</b>	<b>24,071</b>	<b>24,707</b>	<b>25,410</b>	<b>26,186</b>	<b>27,042</b>	<b>27,988</b>
<b>Net Revenue</b>	<b>(7,261)</b>	<b>(5,780)</b>	<b>(4,513)</b>	<b>(3,114)</b>	<b>(1,570)</b>	<b>136</b>	<b>2,019</b>	<b>4,098</b>	<b>6,393</b>	<b>8,927</b>	<b>11,725</b>
<b>Cumulative Net</b>	<b>(7,261)</b>	<b>(32,660)</b>	<b>(57,811)</b>	<b>(76,236)</b>	<b>(87,234)</b>	<b>(90,033)</b>	<b>(83,779)</b>	<b>(67,531)</b>	<b>(40,247)</b>	<b>(779)</b>	<b>52,140</b>

## 2. Financial modelling assumptions

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	HRA Purchasing
Annual Rent Inflation	2% (3% for first 5 years)
Void Loss and bad debt provision	4.00%
Subsidy	3% of total expenditure
Maintenance Costs	£750 per annum
Housing Management Costs	£500 per annum
Inflation	2%
Major Works	£750 per annum
Service charge and ground rent	£1,200 per annum
Net Present Value Discount Rate	3.00%
House Price Inflation	2.5%

Some of the above assumptions have been adjusted from Opendoor Homes modelling assumptions to reflect scheme conditions and market requirements:

- An acquisition fee of 3% has been assumed within the capital cost to cover the cost of delivery

## Appendix C: Initial Risk Register

Ref	Risk type	Risk description	Risk Owner	Date raised	Initial assessment			Control actions	Consequences/ potential impact
					Probability	Impact	RAG		
001	Project management	There is a risk that there is insufficient resource to deliver the project within planned timescales and to meet the scale requirements	Acquisitions Programme Manager	Feb 19	Low	Medium		Project plans and resource planning to be developed to identify key milestones and capacity required to deliver.	Expected savings will not be achieved, and/or project activity will fall behind schedule.
002	Financial	There is a risk that the assumptions made in modelling are not accurate and that the financial benefits are not realised	Acquisitions Programme Manager	Feb 19	Medium	High		Closely monitor activity to track financial benefits and early identification of risks. There are a number of options the Council has, including alternative lettings routes	Rents charged will not be affordable and will impact on the financial viability of the scheme
003	Financial	There is a risk that there will be an insufficient volume of units available for purchase that deliver the required revenue benefits	Acquisitions Programme Manager	Feb 19	Low	High		Where there are no properties available for purchase that meet the modelled average revenue outcome across the whole scheme, no additional units will be acquired.	Delivery of new acquisitions may not be met, if unable to purchase properties at the right price.
004	Financial	There is a risk that legislation, and housing duties will change significantly over the term of the lease and Barnet Homes will have insufficient numbers of suitable applicants to let properties to, increasing void times and impacting on affordability	Acquisitions Programme Manager	Feb 19	Medium	Low		Lettings capacity will be closely monitored and where necessary, TBG will consider other lettings routes for properties acquired	The cost of delivering the scheme will increase

Ref	Risk type	Risk description	Risk Owner	Date raised	Initial assessment			Control actions	Consequences/ potential impact
005	Financial	There is a risk that supply of new stock on the open market will not be sufficient to meet demand	Acquisitions Programme Manager	Feb 19	Medium	Low		Supply of new stock on the market will be closely monitored	Delivery of new acquisitions may not be met, if unable to purchase properties at the right price.
006	Financial	There is a risk that house price inflation will exceed levels anticipated in modelling and impact on the viability of units	Acquisitions Programme Manager	Feb 19	Medium	Low		Where HPI exceeds expectations, further review of the business model will be carried out.	Delivery of new acquisitions may not be met, if unable to purchase properties at the right price.
007	Financial & Reputational	There is a risk that there will be conflicting demands on TBG's acquisition services which in turn impact on the properties sourced for the programme	Acquisitions Programme Manager	Feb 19	Medium	Low		To minimise potential conflict, procurement areas are broadened and particular types of units are prioritised for their respective programmes. Hurdle rates for other programmes will also impact on the ability to acquire in-borough properties, resulting in Barnet properties being prioritised for this programme.	Delivery of new acquisitions may not be met, if unable to purchase properties at the right price.

**Document Control**

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**Distribution List:**

<b>Name</b>	<b>Role</b>	<b>Date</b>
Derek Rust	Deputy CEO, The Barnet Group	14/02/19
Mike Gerrard	Finance Director, The Barnet Group	14/02/19

**Approvals:**

By signing this document, the signatories below are confirming that they have fully reviewed the Business Case for the out-of-borough acquisitions project and confirm their acceptance of the completed document.

<b>Name</b>	<b>Role</b>	<b>Signature</b>	<b>Date</b>	<b>Version</b>