

REFERENCE:
ORGANISATION:
CATEGORY:

016
EAST OF SCOTLAND FINANCE FORUM
OTHER

REF: 16

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Aileen Piacentini
Communities Scotland
Highlander House
58 Waterloo Street
GLASGOW
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25 MAR 2008

20th March 2008

Dear Ms Piacentini

Better Value from HAG Consultation

I am writing to you in my capacity as Chairperson of the East of Scotland Finance Forum (of Housing Associations).

As requested I attach the RIF together with the response of the Forum for your attention.

It is the East of Scotland Finance Forum's hope that the Government will reconsider its proposals and take cognisance of the very serious financial and risk implications set out in the attached précis.

Yours sincerely,



Andrew Clark
Chairperson
East of Scotland Finance Forum

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HAG Consultation Exercise Precis of Discussion at East of Scotland Finance Forum

Background

Rents in Scotland are low in comparison with England therefore scope for them to rise.

HAG per unit has risen by 35% in real terms in last 4 years – unacceptable from Scottish Government point of view.

Resume of Discussion

1. **Borrowing Costs:** Private Finance factor of 21.76458 equates to an interest rate of 4.59%. This is not a rate of interest that the sector is currently able to access. LIBOR (3 month rate) is currently 5.98% and the bank margin of say 35 basis points gives a borrowing cost of 6.33%.
2. **RPI:** Concern expressed over the assumed rate of inflation at 3% which is higher than many associations assume in their 30 year financial projections (currently 2% or 2.5%).
3. **Rents:** The forum could not accept that rents would rise by RPI+1% for the next 30 years when the starting point is already above the Scottish average. Affordability would be a major concern.
4. **Housing Benefit:** Concern was expressed that if housing benefit bore the brunt of the rent increases then this increased the prospect of rent capping or restrictions to housing benefit payouts.
5. **Management & Maintenance Allowances:** The view was expressed by one RSL existing costs could not meet the allowances and no Association present contradicted this view.
6. **Developers:** Associations who developed small sites over a number of local authority areas would be forced to abandon future development ambitions.
7. **HAG Rates:** The old regime produced a HAG:Private Finance split of circa 70:30 and it was generally agreed that the risk : reward balance was favourable to the RSL. However the current proposals produce a split of circa 60:40 and the risk reward ratio moves away from the RSL making it more difficult to justify developing.
8. **Loan Interest Covenant:** Under a 70:30 split developments generally trade at a small loss for the first 5 years then make a positive contribution to the RSL's financial position. Under the 60:40 split the development would trade at a small loss for up to 15 years. This increases the financial risk quite significantly particularly if there is a large development programme. For most traditional RSLs the funders set a covenant of surplus to interest of 110%:100% or 1.1:1.0. This will become more difficult to achieve under the new regime.
9. **Valuation to Loan:** The experience of one RSL was that values from an external valuer produced valuations of £34k to £35k. Under the current regime private finance per unit is circa £25k to £30k. The new regime is predicted to increase private finance by a third so the value to loan cover may not be achieved.

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Impairment Reviews: Under the new regime where the value to loan is 1:1 or worse e.g. 0.9:1.0 the Finance Director or equivalent will be expected to demonstrate to their auditor that there is no impairment i.e. no need to create a provision to reduce the carrying cost of the property to its value (or net realisable value).