

**HOUSING ASSOCIATION FUNDING PLC**

**ANNUAL REPORT AND FINANCIAL STATEMENTS**

**FOR THE YEAR ENDED 31 MAY 2016**

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<b>HOUSING ASSOCIATION FUNDING PLC</b>
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**COMPANY INFORMATION**

<b>DIRECTORS</b>	Sean Martin (appointed 30 July 2015) Capita Trust Corporate Limited Capita Trust Corporate Services Limited Sue Lawrence (resigned 31 July 2015)
<b>COMPANY SECRETARY</b>	Capita Trust Corporate Limited
<b>REGISTERED NUMBER</b>	3194469
<b>REGISTERED OFFICE</b>	4th Floor 40 Dukes Place London EC3A 7NH
<b>INDEPENDENT AUDITOR</b>	Mazars LLP Chartered Accountants and Statutory Auditor Tower Bridge House St Katharine's Way London E1W 1DD

<b>HOUSING ASSOCIATION FUNDING PLC</b>
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## **HOUSING ASSOCIATION FUNDING PLC**

### **STRATEGIC REPORT FOR THE YEAR ENDED 31 MAY 2016**

#### **BUSINESS REVIEW**

Housing Association Funding Plc (the "Company"), registered in England and Wales No. 3194469, is a special purpose company whose only activity is to advance loans to certain Housing Associations and to service notes and bank borrowings issued or raised to finance such advances and is likely to remain so in the foreseeable future. The Housing Association loans have been pledged to Royal Exchange Trust Company Limited as security for the notes.

The Company only operates in the UK and provides funding only to social housing providers.

The Company operated as expected during the year with demand for social housing remaining very high. The rental income for the Housing Associations was 103% (2015: 99%) of the expected £41 million and net rental income was 165% (2015: 169%) of the amount required by the Company to service its debt obligations on the long-term notes. The notes and the loans continued to redeem during the year. The balance of the notes at year end was £135 million (2015: £143 million) and that of the loans was £136 million (2015: £143 million). The cash balance increased to £23 million from £13 million in 2015 mainly due to the drawdown of £9.4million Barclays liquidity facility.

The Government Universal Credit System will become effective in 2017. Currently, most of the eleven housing associations have introduced the Universal Credit system, however at present the number of tenants affected is very low, but this will increase in the near future. There has therefore been no detectable impact so far on the levels of rental collection. This is as expected as the cap on benefits is set at £500 for single parents and for couples and at £350 for single adults. The mean weekly rent across the portfolio was £116 (2015: £107), significantly below the benefits cap, even when living costs are included.

#### **PRINCIPAL RISKS AND UNCERTAINTIES**

The Company's business is predicated on demand for rented housing. Therefore the principal risk facing the Company is based on changes in demographic conditions leading to a significant reduction in the demand to rent the housing which is security for its loan. Demand could reduce if there was an over supply of housing, if the housing was not kept in a good and tenable condition, if the rents for the housing were uncompetitive or, if the housing were located in an undesirable or dangerous area. Management mitigate these risks by ensuring that the dwellings are let and kept in a good and tenable condition. It does this by checking monthly reports of rental collection, which reflect occupancy, against the targets laid down in the loan agreements and by examining the triennial stock condition surveys.

The directors do not currently consider credit risk to be a significant risk to the Company. The reason is that if there is a default by a borrower, the transaction is structured to transfer the management of the charged dwellings allowing the rents to continue to be collected and the dwellings to continue to be managed and maintained and the debt to be serviced out of the rental cash flow. There has not been a default by a borrower in the past seventeen years. The collateral value of the property is not deemed to significantly impact credit risk.

Liquidity is not considered to be a material risk. The Company has an additional facility to ensure the AAA/Aa1 rating of the notes is maintained. If it is not renewed it is held as cash, so there is no exposure to it being withdrawn as long as the Company renews it each year.

There is no interest rate risk as this is a fixed rate transaction.

For more information on the principal risks and how they are managed, please see note 13.

## **HOUSING ASSOCIATION FUNDING PLC**

### **STRATEGIC REPORT (continued) FOR THE YEAR ENDED 31 MAY 2016**

#### **INTERNAL CONTROL AND RISK MANAGEMENT**

Each of the eleven borrowers is obliged under its loan agreement to provide the Company with monthly and quarterly reports about the performance of the dwellings which are charged as security for its borrowing. The administration team monitors the receipt of these investor reports.

Borrowers are also obliged to provide the Company with a solvency certificate every 6 months and an annual certificate confirming the income and rent which has been reported over the preceding year. It is a requirement that the annual certificate be verified by an accompanying auditor's certificate. The administration team also review these certificates and any irregularities are immediately followed up.

#### **FINANCIAL KEY PERFORMANCE INDICATORS**

The loans made to Housing Associations by the Company are serviced out of the rental income generated by a portfolio of social housing properties owned and managed by the Housing Associations. The targets in the Loan Agreements represent the measure to which the Company monitors its business.

The rent collection performance of the property portfolio over the year to 31 May 2016 was 103% (2015: 99%) of the £41 million (2015: £40.2 million) collectible if the properties had been fully occupied and all rents paid on their due date. Overall rent collection performance remains significantly better than the 95% level specified under the Loan Agreements.

As at 31 May 2015 the net rental income (being gross rent less provision for management, maintenance, services and credit losses primarily from empty dwellings) of the properties charged to the Company was 165% (2015: 169%) of the amount required by the Company to service its debt obligations on the long-term notes. Overall debt service remains significantly higher than the 105% level specified under the Loan Agreements between the Company and the relevant Housing Associations.

#### **STRATEGY & FUTURE DEVELOPMENT**

The strategy of the Company is to ensure that it continues to service its debt obligations under the notes in a full and timely manner up to and including the final maturity of the Notes in June 2027.

#### **FINANCIAL INSTRUMENTS**

The Company's principal financial instruments comprise lending to Housing Associations and borrowings that arise directly from its operations. The main purpose of these borrowings is to raise finance for the Company's operations. Further information regarding the risks arising from the use of all the Company's financial instruments is included within Note 13. It is, and has been throughout the year under review, the Company's policy that no trading in financial instruments shall be undertaken. The Board reviews and agrees the policy for managing the financial risk profile of the Company.

This report was approved by the board on 6 October 2016 and signed on its behalf.

**David Osborne**  
for and on behalf of  
**Capita Trust Corporate Services Limited**  
Director



## **HOUSING ASSOCIATION FUNDING PLC**

### **DIRECTORS' REPORT FOR THE YEAR ENDED 31 MAY 2016**

The directors present their report and the audited financial statements for the year ended 31 May 2016.

#### **DIVIDENDS**

The directors do not recommend the payment of a dividend for the current year (2015: nil).

#### **DIRECTORS**

The directors who served during the year were as follows:

Sean Martin (appointed 30 July 2015)  
Capita Trust Corporate Limited  
Capita Trust Corporate Services Limited  
Sue Lawrence (resigned 31 July 2015)

#### **EVENTS SINCE THE END OF THE YEAR**

There were no significant post balance sheet events.

#### **CORPORATE GOVERNANCE STATEMENT**

The Directors have a supervisory role in overseeing the business, strategic direction, organisational structure and risk management activities of the Company. The Director membership represents an appropriate mix of experience and knowledge relevant to the Company's business lines. Board meetings are held at least four times a year, and additional meetings can be held at any time to discuss urgent issues. The day-to-day activities of the Company are controlled by Capita Trust Corporate Limited.

#### **GOING CONCERN**

Barclays Bank Plc is the Account Bank and Liquidity Facility Provider in this transaction. On 9 June 2015, Standard & Poor's Ratings Services lowered its rating of Barclays Bank Plc to 'A-/A-2' following Government Support a ALAC Review. The full commitment of £9.4 million under the Additional Facility Agreement has been drawn down under the terms of the transaction documentation, and placed in an account held with Barclays Bank Plc. These funds can be used to cover shortfalls in the amounts available to be used by the issuer to meet its obligations on the notes.

The noteholders will be asked to vote on novating the Account Bank role to an appropriately rated bank which has a higher credit rating than Barclays Bank Plc.

On 8 October 2015, Standard & Poor's Ratings Services ('S&P') lowered and placed on CreditWatch negative its credit ratings on Housing Association Funding PLC's class A, B, C, and D notes. The downgrades reflect S&P's view that principal and interest due on the notes would not be timely paid under in their 'AAA' cash flow scenario. Under S&P's credit and cash flow analysis, the notes can withstand the stresses applied at the 'AA+' rating. Therefore S&P lowered to 'AA+' from 'AAA' ratings on the class A, B, C, and D notes.

The downgrade of the notes is not expected to have any operational impact on the Company.

The UK Government has introduced new legislation pursuant to which rents chargeable by Housing Associations on their social housing in England must reduce by 1% per annum for the next four years instead of increasing by CPI +1% per annum over the same period. This change was introduced on 1 April 2016 pursuant to Section 20 of the Act. The wording of Section 20 of the Act is as follows:

"In relation to each relevant year, registered providers of social housing must secure that the amount of rent payable in respect of that relevant year by a tenant of their social housing in England is at least 1% less than the amount of rent that was payable by the tenant in respect of the preceding 12 months"

## **HOUSING ASSOCIATION FUNDING PLC**

### **DIRECTORS' REPORT FOR THE YEAR ENDED 31 MAY 2016**

This rent reduction will apply to tenants of properties which are currently charged as security by the Borrowers in favour of the Issuer pursuant to the Legal Charges (the Charged Properties).

Although the Act has now come into force, none of the Borrowers apart from one have reduced their rents on any of the Charged Properties as a result or in anticipation of the implementation of the Act. Under the Act there was no requirement to reduce rents on 1 April 2016. The Borrowers other than one are intending to defer the required reduction until later in 2016 and then introduce a higher reduction in rent so that a 1% reduction across the year 1 April 2016- 31 March 2017 is achieved.

Midland Heart Limited has confirmed to the Issuer that it has reduced the rents of those of its Charged Properties affected by the implementation of the Act, where anniversary increases were due, by 1% per annum with effect from 1 April 2016.

The issuer and the and the borrowers have sought legal advice as to whether this could trigger a material event of default.

The Company continues to satisfy all its key performance indicators and to make its payments to noteholders in full and on time without recourse to its additional facility. This is as expected. Looking forward, historic data shows that demand for rented housing of the type which is the security for the Company's loans and the hypothecated source of its cash flow, is very high. Furthermore, the Company has the benefit of a £9.4 million 364-day additional facility, equivalent to more than six months' debt service for the Company (and equivalent to more than two years' debt service for any one of the Housing Associations) if this is required. Based on this information, the directors have no reason to believe that the Company will not meet its liabilities as they fall due. Consequently the going concern basis continues to be appropriate in preparing the financial statements.

Please refer to the Strategic Report, principal risks and uncertainties on Government Universal Credit System.

#### **QUALIFYING THIRD PARTY INDEMNITY PROVISIONS**

The Company has made qualifying third party indemnity provisions for the benefit of the directors. These indemnity provisions remain in force at the date of this report.

#### **MATTERS COVERED IN THE STRATEGIC REPORT**

As permitted in paragraph 1A of Schedule 7 to Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 certain matters which are required to be disclosed in the Directors' Report have been omitted as they are included in the Strategic Report on pages 1 and 2. These matters relate to the business review, financial instruments, future developments and financial risk management and policies.

#### **DISCLOSURE OF INFORMATION TO AUDITOR**

Each of the persons who are directors at the time when this Directors' Report is approved has confirmed that:

- so far as the director is aware, there is no relevant audit information of which the Company's auditor is unaware, and
- the director has taken all the steps that ought to have been taken as a director in order to be aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

It is not considered appropriate to have an audit committee as the sole business of the Company is to act as the issuer of Asset Backed Securities.

**HOUSING ASSOCIATION FUNDING PLC**

**DIRECTORS' REPORT  
FOR THE YEAR ENDED 31 MAY 2016**

**INDEPENDENT AUDITOR**

The auditor, Mazars LLP, will be proposed for reappointment in accordance with section 489 of the Companies Act 2006.

This report was approved by the board on 6 October 2016 and signed on its behalf.

  
**David Osborne**  
for and on behalf of  
**Capita Trust Corporate Limited**  
Director



<b>HOUSING ASSOCIATION FUNDING PLC</b>
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**DIRECTORS' RESPONSIBILITIES STATEMENT  
FOR THE YEAR ENDED 31 MAY 2016**

The directors are responsible for preparing the Strategic Report, the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland". Under company law the directors must not approve the financial statements unless they are satisfied that: they give a true and fair view of the state of affairs of the company and the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements ;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

## **HOUSING ASSOCIATION FUNDING PLC**

### **INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF HOUSING ASSOCIATION FUNDING PLC**

We have audited the financial statements of Housing Association Funding Plc for the year ended 31 May 2016 set out on pages 9 to 24 which comprise the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Changes in Equity, the Statement of Cash Flows and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Generally Accepted Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland".

#### **RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITOR**

As explained more fully in the Directors' Responsibilities Statement set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Financial Reporting Council's Ethical Standards for Auditors.

This report is made solely to the Company's member as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body for our audit work, for this report, or for the opinions we have formed.

#### **SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS**

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at [www.frc.org.uk/auditscopeukprivate](http://www.frc.org.uk/auditscopeukprivate).

#### **OPINION ON FINANCIAL STATEMENTS**

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 May 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

#### **OPINION ON OTHER MATTER PRESCRIBED BY THE COMPANIES ACT 2006**

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

**HOUSING ASSOCIATION FUNDING PLC**

**INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF HOUSING ASSOCIATION FUNDING PLC**

**MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.



Greg Simpson (Senior Statutory Auditor)

for and on behalf of  
**Mazars LLP**

Chartered Accountants and Statutory Auditor  
Tower Bridge House  
St Katharine's Way  
London  
E1W 1DD

6 October 2016

# HOUSING ASSOCIATION FUNDING PLC

## STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 MAY 2016

	Note	2016 £	2015 £
Interest receivable on Housing Association loans and bank balances	4	9,711,369	10,193,999
Interest payable on notes		(9,703,619)	(10,185,836)
<b>GROSS PROFIT</b>		<b>7,750</b>	<b>8,163</b>
Administrative expenses		(689,924)	(180,304)
Fees receivable		689,876	180,304
<b>Profit on ordinary activities before taxation</b>		<b>7,702</b>	<b>8,163</b>
Tax on profit on ordinary activities	6	(1,541)	(1,633)
<b>TOTAL COMPREHENSIVE INCOME FOR THE YEAR</b>		<b>6,161</b>	<b>6,530</b>

All amounts relate to continuing operations.

The notes on pages 13 to 24 form part of these financial statements.

# HOUSING ASSOCIATION FUNDING PLC

## STATEMENT OF FINANCIAL POSITION AS AT 31 MAY 2016

	Note	£	2016 £	£	2015 £
<b>FIXED ASSETS</b>					
Housing Association loans	7		127,485,058		135,458,695
<b>CURRENT ASSETS</b>					
Debtors	8	12,980,890		12,492,324	
Cash at bank and in hand	9	23,498,960		13,478,628	
		<u>36,479,850</u>		<u>25,970,952</u>	
<b>CREDITORS: amounts falling due within one year</b>	10	<u>(36,192,593)</u>		<u>(25,671,468)</u>	
<b>NET CURRENT ASSETS</b>			<u>287,257</u>		<u>299,484</u>
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>			<u>127,772,315</u>		<u>135,758,179</u>
<b>CREDITORS: amounts falling due after more than one year</b>	11		<u>(127,574,255)</u>		<u>(135,566,280)</u>
<b>NET ASSETS</b>			<u>198,060</u>		<u>191,899</u>
<b>CAPITAL AND RESERVES</b>					
Called up share capital			50,000		50,000
Profit and loss account			<u>148,060</u>		<u>141,899</u>
<b>SHAREHOLDERS' EQUITY</b>			<u>198,060</u>		<u>191,899</u>

The financial statements were approved and authorised for issue by the board and were signed on its behalf on 6 October 2016.



**David Osborne**  
for and on behalf of  
**Capita Trust Corporate Limited**  
Director

The notes on pages 13 to 24 form part of these financial statements.

# HOUSING ASSOCIATION FUNDING PLC

## STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 MAY 2016

	Called up share capital £'000	Profit and loss account £'000	Shareholder's equity £'000
As at 1 June 2014	50,000	135,369	185,369
Other comprehensive income	-	-	-
Total comprehensive income for the year	<u>-</u>	<u>6,530</u>	<u>6,530</u>
As at 31 May 2015	<u>50,000</u>	<u>141,899</u>	<u>191,899</u>
As at 1 June 2015	50,000	141,899	191,899
Other comprehensive income	-	-	-
Total comprehensive income for the year	<u>-</u>	<u>6,161</u>	<u>6,161</u>
As at 31 May 2016	<u><u>50,000</u></u>	<u><u>148,060</u></u>	<u><u>198,060</u></u>

### Profit and loss account

This reserve represents cumulative profits and losses of the Company.

The notes on page 13 to 24 form part of these financial statements.

# HOUSING ASSOCIATION FUNDING PLC

## STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 MAY 2016

	2016 £	2015 £
<b>Operating activities</b>		
Profit before taxation	7,702	8,163
Decrease in debtors	11,893	224,921
Increase in creditors	<u>549,021</u>	<u>986,467</u>
<b>Cash (inflow) from operating activities before tax</b>	<b>568,616</b>	<b>1,219,551</b>
UK Corporation tax paid	<u>(1,633)</u>	<u>(1,699)</u>
<b>Net cash (outflow) from operating activities</b>	<b>566,983</b>	<b>1,217,852</b>
<b>Cash flow from investing activities</b>		
Redemption of loans	<u>7,473,178</u>	<u>6,981,497</u>
<b>Net cash inflow from investing activities</b>	<b>7,473,178</b>	<b>6,981,497</b>
<b>Cash flow from financing activities</b>		
Liquidity facility from Barclays	9,441,257	-
Redemption of loan notes	<u>(7,461,086)</u>	<u>(6,984,357)</u>
<b>Net cash (outflow)/inflow from financing activities</b>	<b>1,980,171</b>	<b>(6,984,357)</b>
<b>Net (decrease)/increase in cash</b>	<u><b>10,020,332</b></u>	<u><b>1,214,992</b></u>
<b>Cash and cash equivalents at the beginning of the year</b>	<u><b>13,478,628</b></u>	<u><b>12,263,636</b></u>
<b>Cash and cash equivalents at end of the year</b>	<u><b>23,498,960</b></u>	<u><b>13,478,628</b></u>

The notes on page 13 to 24 form part of these financial statements.

## HOUSING ASSOCIATION FUNDING PLC

### NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

#### 1. GENERAL INFORMATION

The Company has debt listed on the London Stock Exchange and is registered in England and Wales with registration number 3194469. The address of its registered office and principal place of business is :

4th Floor, 40 Dukes Place, London EC3A 7NH

#### 2. ACCOUNTING POLICIES

A summary of the principal accounting policies, all of which have been applied consistently throughout the year, is set out below:

##### 2.1 Basis of preparation and transition to FRS102

These financial statements have been prepared in accordance with FRS 102 The Financial Reporting Standard Applicable in the UK and Republic of Ireland ("FRS 102") and applicable legislation, as set out in the Companies Act 2006. These financial statements have been prepared under the historical cost convention.

The financial statements for the year ended 31 May 2016 are the Company's first financial statements that comply with FRS 102; the Company's date of transition to FRS 102 is 1 June 2014. Note 18 describes the impact on reported profit or loss and equity upon transition to FRS 102.

In accordance with paragraph 4(1) of Schedule 1 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, the directors have adapted the arrangement of certain headings in the profit and loss account to reflect more accurately the nature of the Company's activities. A summary of important and material accounting policies is set out below.

##### 2.2 Going concern

Barclays Bank Plc is the Account Bank and Liquidity Facility Provider in this transaction. On 9 June 2015, Standard & Poor's Ratings Services lowered its rating of Barclays Bank Plc to 'A-/A-2' following Government Support a ALAC Review. The full commitment of £9.4 million under the Additional Facility Agreement has been drawn down under the terms of the transaction documentation, and placed in an account held with Barclays Bank Plc. These funds can be used to cover shortfalls in the amounts available to be used by the issuer to meet its obligations on the notes.

The noteholders will be asked to vote on novating the Account Bank role to an appropriately rated bank which has a higher credit rating than Barclays Bank Plc.

On 8 October 2015, Standard & Poor's Ratings Services ('S&P') lowered and placed on CreditWatch negative its credit ratings on Housing Association Funding PLC's class A, B, C, and D notes. The downgrades reflect S&P's view that principal and interest due on the notes would not be timely paid under in their 'AAA' cash flow scenario. Under S&P's credit and cash flow analysis, the notes can withstand the stresses applied at the 'AA+' rating. Therefore S&P lowered to 'AA+' from 'AAA' ratings on the class A, B, C, and D notes.

The downgrade of the notes is not expected to have any operational impact on the Company.



## HOUSING ASSOCIATION FUNDING PLC

### NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

#### 2. ACCOUNTING POLICIES (continued)

##### Going concern ( continued)

The UK Government has introduced new legislation pursuant to which rents chargeable by Housing Associations on their social housing in England must reduce by 1% per annum for the next four years instead of increasing by CPI +1% per annum over the same period. This change was introduced on 1 April 2016 pursuant to Section 20 of the Act. The wording of Section 20 of the Act is as follows:

"In relation to each relevant year, registered providers of social housing must secure that the amount of rent payable in respect of that relevant year by a tenant of their social housing in England is at least 1% less than the amount of rent that was payable by the tenant in respect of the preceding 12 months"

This rent reduction will apply to tenants of properties which are currently charged as security by the Borrowers in favour of the Issuer pursuant to the Legal Charges (the Charged Properties).

The issuer and the borrowers have sought legal advice as to whether this could trigger a material event of default.

The Company continues to satisfy all its key performance indicators and to make its payments to noteholders in full and on time without recourse to its additional facility. The Company has the benefit of a £9.4 million 364-day additional facility, equivalent to more than six months' debt service for the Company (and equivalent to more than two years' debt service for any one of the Housing Associations) if this is required. Based on this information, the directors have no reason to believe that the Company will not meet its liabilities as they fall due. Consequently the going concern basis continues to be appropriate in preparing the financial statements.

##### 2.3 Value added tax

Value added tax is not recoverable by either the Company or the Group and is included with its related cost.

##### 2.4 Interest

Interest receivable and interest payable are recognised in the profit and loss account using the effective interest method.

The effective interest method is a method of allocating the interest income or interest expense evenly in proportion to the amount outstanding over the period to maturity or repayment. The effective interest rate is the rate that exactly discounts the expected future cash payments or receipts through the expected life of the financial instrument, or when appropriate, a shorter period, to the net carrying amount of the instrument.

##### 2.5 Fees receivable

Fees recognised in the financial statements relate to the recharge of administrative costs incurred by the Company. These costs are recharged to the Housing Associations. Fees receivable are recognised on an accruals basis in the year in which the costs have been incurred.

##### 2.6 Taxation

The Company has elected to be taxed under the Taxation for Securitisation Companies 2006 (Regulations) ie, the permanent regime. Corporation tax is therefore calculated by reference to the profit of the securitisation company required to be retained in accordance with the relevant capital market arrangements.

## HOUSING ASSOCIATION FUNDING PLC

### NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

## 2. ACCOUNTING POLICIES (continued)

### 2.7 Segmental analysis

The Company only operates in the UK and there are no reportable segments which are managed separately based on the Company's management and internal reporting structure.

### 2.8 Financial instruments

Financial assets and liabilities are recognised when the company becomes party to the contractual provisions of the financial instrument. The company holds only basic financial instruments, which comprise cash and cash equivalents, trade and other debtors, and trade and other creditors. The company has chosen to apply the measurement and recognition provisions of Section 11 Basic Financial Instruments and Section 12 Other Financial Instrument Issues in full.

#### Financial assets – classified as basic financial instruments

##### Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, deposits held with banks and other short-term highly liquid investments with original maturities of three months or less.

##### Trade and other debtors and investments

Trade and other debtors are initially recognised at the transaction price, including any transaction costs, and are subsequently measured at amortised cost using the effective interest method, less any provision for impairment.

Amounts that are receivable within one year are measured at the undiscounted amount expected to be receivable, net of any impairment.

Where a financial asset constitutes a financing transaction it is initially and subsequently measured at the present value of the future payments, discounted at a market rate of interest.

At each reporting date, the company assesses whether there is objective evidence that any financial asset may be impaired. A provision for impairment is established when there is objective evidence that the company will not be able to collect all amounts due according to the original terms of the financial asset. The amount of the provision is the difference between the asset's carrying amount and the present value of the estimated future cash flows. The amount of the provision is recognised immediately in profit or loss.

### 2.9 Financial liabilities measured at amortised cost

A financial liability is any liability that is a contractual obligation to deliver cash or another financial asset to another entity. Financial liabilities are initially measured at their transaction price, including any transaction costs and are subsequently amortised cost using the effective interest rate method.

The Company's financial liabilities include notes listed on the London Stock Exchange with final maturity of June 2027. The notes are non-derivative financial liabilities with fixed or determinable payments. Liabilities are initially measured at fair value and subsequently measured at amortised cost, using the effective interest method. They are derecognised when the Company has paid all of the cash flows due on the notes (including principal) or is legally released from primary responsibility for the liability (or part of it) either by process of law or by the noteholders.

# HOUSING ASSOCIATION FUNDING PLC

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

### 2. ACCOUNTING POLICIES (continued)

#### 2.10 Critical accounting estimates and judgements

The preparation of the Company financial statements in accordance with FRS 102 requires management to make judgements, estimates and assumptions in applying accounting policies that affect the reported amounts of assets, liabilities, income and expenses. Due to the inherent uncertainty in making estimates, actual results reported in future periods may be based upon amounts which differ from those estimates. Estimates, judgements and assumptions are continually evaluated and based on historical experience and factors, including expectations of future events that are believed to be reasonable under the circumstances.

The significant judgements made by management in applying the Company's accounting policies and the key sources of estimation uncertainty in these financial statements, which together are deemed critical to the Company's results and financial position, are as follows:

(i) Determining the fair value of financial instruments (*Note: 13*)

Where the fair value of financial instruments cannot be reasonably determined by a reference to an active market, the valuation technique is used including a discounted cash flow model where the inputs to this model are taken from observable markets where possible. However where this is not feasible, a degree of judgement is required in establishing fair values.

### 3. PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

Profit on ordinary activities before taxation is stated after charging:	2016 £	2015 £
Audit of the annual financial statements of the Company	22,200	19,579
Administrative expenses	689,924	180,304
	<hr/>	<hr/>

During the year the Company accrued audit fees of £2,600 (2015: £2,591) for Housing Association Funding Limited, these fees are not recharged.

The administrative expenses increased significantly during the year due to ongoing legal work. The legal work related to the following:

- Proposed transfer of roles in accordance with the terms of a Deed of Novation and Transfer (yet to be entered into) following the downgrade of Barclays Bank plc's short-term counterparty credit ratings from 'A-1' to 'A-2', and their long-term credit ratings from 'A' to 'A-';
- Advice relating to the Material Events EoD clause following the introduction of Section 20 of the Welfare Reform and Work Act 2016;
- Proposed amendment of the Loan Agreements and Transaction Documentation; and General advice.

### 4. INTEREST INCOME

Interest income comprises:	2016 £	2015 £
Interest receivable on Housing Association loans	9,711,279	10,193,894
Interest receivable on cash and bank balances	90	105
Total	<hr/> <hr/>	<hr/> <hr/>

# HOUSING ASSOCIATION FUNDING PLC

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

### 5. DIRECTORS' REMUNERATION

#### Directors

The following were directors of the Company during the year, Capita Trust Corporate Services Limited, Capita Trust Corporate Limited and Sean Martin. Capita Trust Corporate Services Limited received £8,898 (2015: £8,874) for the provision of the services of two directors based on a schedule set out in 1997. No other remuneration was paid to the directors for the year ended 31 May 2016 (2015: £nil).

#### Employees

No employees were employed by the Company during the year ended 31 May 2016 (2015: none).

### 6. TAX ON PROFIT ON ORDINARY ACTIVITIES

	2016 £	2015 £
UK corporation tax charge on profit for the year	<u>1,541</u>	<u>1,633</u>

#### Factors affecting tax charge for the year

The tax assessed for the year is the same as (2015 - the same as) the standard rate of corporation tax in the UK of 20% (2015 - 20%):

#### Factors affecting tax charge for the year (continued)

	2016 £	2015 £
Tax on profit		
Profit on ordinary activities before tax	<u>7,702</u>	<u>8,163</u>
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 20% (2015: 20%)	1,541	1,633
Total tax	<u>1,541</u>	<u>1,633</u>

The Company has elected to enter the permanent tax regime for securitisation companies. The directors are satisfied that the Company meets the definition of a 'securitisation company' as defined by both. The Finance Act 2005 and subsequent secondary legislation and that no incremental unfunded tax liabilities will arise.

The directors are satisfied that the Company currently satisfies the conditions to be taxed under the permanent regime.

# HOUSING ASSOCIATION FUNDING PLC

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

### 7. HOUSING ASSOCIATION LOANS - Amounts falling due after one year

	2016 £	2015 £
Balance as at 1 June	135,458,695	142,931,873
Loans due in one year (see note 8)	(7,973,637)	(7,473,178)
	<u>127,485,058</u>	<u>135,458,695</u>
Balance as at 31 May		
<b>Repayable as follows:</b>		
In more than one year but not more than five years	38,066,422	35,535,460
In more than five years	89,418,636	99,923,235
	<u>127,485,058</u>	<u>135,458,695</u>
Balance as at 31 May		

There is currently a dispute between the arranger and borrowers as to whether the rent reduction could trigger a material event of default which could result in the modification of the transaction. Until this dispute is resolved, the directors continue to consider the maturity profile of the housing association loans to follow the current contractual repayment profile.

### 8. DEBTORS - Amounts falling due within one year

	2016 £	2015 £
Accrued interest	4,655,457	4,880,628
Share capital due	37,498	37,498
Housing association loans	7,973,637	7,473,178
Amounts recoverable from Housing Associations	314,298	101,020
	<u>12,980,890</u>	<u>12,492,324</u>

The Company has not recognised any allowances against debtors and there are no amounts past due on the amounts set out above.

### 9. CASH AT BANK AND IN HAND

	2016 £	2015 £
Amounts held on behalf of Housing Associations	14,042,599	13,426,539
Operating account	15,104	52,089
Amounts held on behalf of Barclays	9,441,257	-
Total	<u>23,498,960</u>	<u>13,478,628</u>

Amounts held on behalf of Housing Associations can only be used to pay the interest due on the notes on each interest payment date. Any balance left after payment of the note interest is repaid to the Housing Associations.

In accordance with the additional facility, as a result of the Barclays downgrade, the company has drawdown the facility of £9.4m.

# HOUSING ASSOCIATION FUNDING PLC

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

### 10. CREDITORS:

Amounts falling due within one year

	2016 £	2015 £
Amounts due to Housing Associations and Barclays	23,484,136	13,426,819
Corporation tax	1,541	1,633
Other creditors	208,453	41,360
Debt in issue at amortised cost	7,994,625	7,461,086
Accrued interest	4,503,838	4,740,570
	<u>36,192,593</u>	<u>25,671,468</u>

### 11. CREDITORS - Amounts falling due after more than one year

	2016 £	2015 £
Debt in issue at amortised cost	127,574,255	135,566,280
	<u>127,574,255</u>	<u>135,566,280</u>
<b>Repayable</b>		
In more than one year but not more than five years	38,086,105	35,556,641
In more than five years	89,488,150	100,009,639
	<u>127,574,255</u>	<u>135,566,280</u>

The Notes are repayable by equal semi-annual instalments of principal and interest on 7th June and 7th December in each year up to and including 7th June 2027 at the effective interest rates shown in note 13. The debt is secured against the loans to the Housing Associations.

### 12. Share Capital

The Company has 50,000 ordinary shares at £1 each. Each share is entitled to one voting rights. £2 have been allocated and fully paid for and £49,998 have been allotted and partially paid for. These shares do not have rights to dividends or preferences.

## HOUSING ASSOCIATION FUNDING PLC

### NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

#### 13. FINANCIAL INSTRUMENTS

##### Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. On the basis that the interest rates on the principal financial assets and financial liabilities are fixed, the only exposure to cash flow interest rate risk is on cash balances, which are subject to variable rates of interest. As set out in note 9, the Company's own cash balances throughout the year are not significant therefore the exposure to interest rate risk is minimal.

The Company has securitised receivables which consist of a portfolio of fixed rate loans to Housing Associations. The Company finances its operations through the issue of long term notes. The notes are denominated in sterling at fixed rates. The directors believe that the Company's exposure to both fair value and cash flow interest rate risk has been minimised due to the loans and notes being at fixed interest rates and same repayment terms.

##### Notes

Interest on the fixed rate liabilities is determined and payable on a semi annual basis at the following rate:

	Carrying value 2016 £	Carrying value 2015 £	Effective rate
1997: 68,250,000 8.25% notes	44,847,379	46,778,862	8.55%
1998: 64,600,000 8.25% notes	45,706,850	48,029,347	7.03%
2001: 28,100,000 8.25% notes	20,626,189	21,751,910	6.30%
2005: 31,320,000 8.25% notes	24,385,862	26,187,435	4.93%

The difference between the coupon rate and effective rate on the notes is due to the notes being issued at a premium/discount.

##### Loans

Interest on the fixed rate assets is determined and payable on a semi annual basis at the following rates:

	Carrying value 2016 £	Carrying value 2015 £	Effective rate
1997	44,652,832	46,778,862	8.57%
1998	45,571,171	48,029,347	7.03%
2001	20,584,523	21,751,910	6.31%
2005	24,650,168	26,187,435	4.94%

The directors believe that the Company's overall exposure to interest rate risk is insignificant and therefore interest rate sensitivity analysis has not been performed.

##### Foreign currency risk

Foreign currency risk is the risk of exposure to changes in exchange rates. The Company is not exposed to any foreign exchange risk as all assets and liabilities of the Company are denominated in sterling and the Company does not carry out any transactions in foreign denominated currencies.

# HOUSING ASSOCIATION FUNDING PLC

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

### 13. Financial instruments (continued)

#### Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Under its Loan Agreement, each Housing Association has granted security in respect of its own obligations to Housing Association Funding Plc. The underlying security of each Housing Association includes a legal charge over its property portfolio. This constitutes a first priority legal mortgage, an assignment by way of security of the benefit of all insurance monies arising in respect of the relevant borrower's title to the portfolio and a charge on the relevant buildings insurance monies. The net rental income of the properties charged to Housing Association Funding Plc is monitored on a monthly and quarterly basis to ensure that the Housing Associations are able to service their debt on the loans. If there is a default by a borrower, the transaction is structured to transfer the management of the charged dwellings allowing the rents to continue to be collected and the dwellings to continue to be managed and maintained and the debt to be serviced out of the rental cash flow. Consequently, management assess the quality of the underlying security of each Housing Association rather than performing credit checks on the Housing Associations when arranging the Loan Agreements.

The notes issued by the Company were rated AAA/Aa1 by Standard & Poor's and Moody's Investors Service Ltd respectively. The ratings reflect the high credit quality of the underlying collateral (i.e. the debt servicing capacity of the rental cash flows from the dwellings which are charged as security) rather than the credit standing of each of the participating Housing Associations.

The maximum exposure to credit risk arising on the Company's financial assets at 31 May 2016 is disclosed in the table below:

Assets	Carrying value 2016 £	Maximum exposure 2016 £
Loans	135,458,695	135,458,695
Other receivables	5,007,253	5,007,253
Cash at bank and in hand	14,057,703	14,057,703

The maximum exposure to credit risk arising on the Company's financial assets at 31 May 2015 is disclosed in the table below:

Assets	Carrying value 2015 £	Maximum exposure 2015 £
Loans	142,931,873	142,931,873
Other receivables	5,019,146	5,019,146
Cash at bank and in hand	13,478,628	13,478,628

Liquidity risk is the risk that the Company is unable to make payment to its creditors in full and on time. The Company has the benefit of a £9.4 million 364-day additional facility, equivalent to more than six months debt service for the Company (and equivalent to more than two years' debt service for any one of the Housing Associations). The same facility and amount was also available in 2015.



# HOUSING ASSOCIATION FUNDING PLC

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

### 13. FINANCIAL INSTRUMENTS (continued)

#### Liquidity risk

The table below reflects the undiscounted contractual cash flows of financial liabilities at the reporting date.

	2016 £	2015 £
In one year or less, or on demand	44,152,772	30,871,249
In more than one year, but no more than two years	17,401,437	17,401,437
In more than two years but no more than five years	52,204,310	52,204,310
In more than five years	113,109,338	130,510,775
Total	<u>226,867,857</u>	<u>230,987,771</u>

#### Financial assets

The financial assets of the Company comprise loans to Housing Associations (including accrued interest), cash at bank balances, amounts recoverable from Housing Associations and share capital due. Loans to Housing Associations and cash at bank balances are interest bearing and are at fixed and variable rates respectively. The cash at bank balances are available on demand.

#### Book value and fair value of financial assets

Loans and receivables	2016 Book value £	2016 Fair value £	2015 Book value £	2015 Fair value £
Housing Association loans	135,458,695	168,884,712	142,931,873	185,076,788
Accrued interest	4,655,457	4,655,457	4,880,628	4,880,628
Cash at bank and in hand	23,498,960	23,498,960	13,478,628	13,478,628
Amounts recoverable from Housing Associations	314,298	314,298	101,020	101,020
Share capital due	<u>37,498</u>	<u>37,498</u>	<u>37,498</u>	<u>37,498</u>
Total	<u>163,964,908</u>	<u>197,390,925</u>	<u>161,429,647</u>	<u>203,574,562</u>

The fair value of the Loans is derived by cash flow analysis discounted by yield to maturity on the notes as at 31 May 2016.

#### Financial liabilities

The financial liabilities of the Company comprise debt in issue (including accrued interest) together with certain amounts held on behalf of the Housing Associations. The assets and liabilities of the Company are based on fixed interest rates and the same repayment terms.

# HOUSING ASSOCIATION FUNDING PLC

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

### 13. FINANCIAL INSTRUMENTS (continued)

Book value and fair value of financial liabilities

Financial liabilities at amortised cost

	2016 Book value £	2016 Fair value £	2015 Book value £	2015 Fair value £
Debt in issue	135,566,280	168,805,253	143,027,366	184,989,711
Amounts due to Housing Associations	14,042,879	14,042,879	13,426,819	13,426,819
Accrued interest	4,503,838	4,503,838	4,740,570	4,740,570
Other creditors	211,053	211,053	42,993	42,993
Amounts due to Barclays	9,441,257	9,441,257	-	-
<b>Total</b>	<b>163,765,307</b>	<b>197,004,280</b>	<b>161,237,748</b>	<b>203,200,093</b>

The fair value of the notes is derived from quoted yield to maturity as at 31 May 2016. The fair value of the loans is derived from cash flow analysis discounted at the same yield as the notes since the quoted price of the notes depends on the performance of the loans.

The Company classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- a) quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);
- b) inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly (derived from prices) (Level 2); and
- c) inputs for the asset or liability that are not based on observable market data (unobservable inputs) (Level 3).

The notes are classified as level 1 since they are valued using quoted prices.

The loans are classified as level 2 since they are valued using observable market data.

### 14. Capital Management

The Company considers its capital to comprise its ordinary share capital and its accumulated retained earnings. The primary objective of this special purpose company is to ensure the obligations to the noteholders are met and to monitor the cash flows from the borrowing Housing Associations. In order to achieve its objectives in this area, the Company seeks to maintain a capital structure appropriate to its size and the underlying risk of the entity.

### 15. ULTIMATE PARENT UNDERTAKING AND CONTROLLING PARTY

The Company is a subsidiary of Housing Association Funding Limited which is registered in England and Wales with registered number 3230346. Financial statements are prepared for Housing Association Funding Limited. Copies may be obtained from its registered office at Housing Association Funding Limited, 4th Floor, 40 Dukes Place, London, EC3A 7NH.

The issued share capital of the parent company is held by Royal Exchange Trust Company Limited subject to a declaration of trust ultimately for charitable purposes. The directors therefore consider Housing Association Funding Limited to be the ultimate controlling party.

## HOUSING ASSOCIATION FUNDING PLC

### NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 MAY 2016

#### 16. RELATIONSHIP OF CORPORATE DIRECTOR TO CORPORATE TRUSTEE

The directors of the Company and the corporate secretary are either employed by, or are provided by, companies whose ultimate parent is Capita Plc, a company listed on the London Stock Exchange. The fees for these services are borne by the Housing Associations.

#### 17. RELATED PARTY TRANSACTIONS

The directors of the Company are shown on page 3 of this Annual Report. As well as the fees received for director services of £8,898 (2015: £8,874) (see note 5), Capita Trust Company Limited received the following fees during the year for services rendered to Housing Association Funding Plc: administration manager services for £19,253 (2015: £75,391), services relating to the provision of Note Trustee £13,759 (2015: £13,532), and additional services of £65,937 (2015: £6,000). The total amount paid to Capita Trust Company Limited during the year was £107,847 (2015: £106,940). At year-end, £4,449 was pre-paid (2015: £4,473) and £18,319 was accrued (2015: £13,925). The directors of the Company received no remuneration for the year ended 31 May 2016 (2015: nil).

During the year the Company paid for audit fees of £2,600 (2015: £2,591) for Housing Association Funding Limited, these fees are not recharged.

#### 18. POST BALANCE SHEET EVENTS

There have been no significant events affecting the Company since the year end.

#### 19. TRANSITION TO FRS 102

This is the first financial year that the Company has presented its financial statements in accordance with FRS 102 "The Financial Reporting Framework Applicable in the UK and Republic of Ireland" ("FRS 102"). For financial years up to and including the year ending 31 May 2015, the company prepared its financial statements in accordance with old UK GAAP.

The company's date of transition to FRS 102 is therefore 1 June 2014. This note sets out the changes to accounting policies and the transitional adjustments that are required to be made for first-time transition to FRS 102. The company's opening equity position as at the 1 June 2014 and its previously published financial statements for the year ended 31 May 2015 have been restated from old UK GAAP. In carrying out the transition to FRS 102, the Company has not applied any of the exemption permitted by Section 35 Transition to this FRS.

There are no adjustments resulting from the transition from previous GAAP to FRS102 which affect the statement of comprehensive income or the statement of financial position.