

BABERGH DISTRICT COUNCIL

FROM: Director of Finance and Head
of Community Development

REPORT NUMBER **K64**

TO: STRATEGY COMMITTEE

DATE OF MEETING 29 July 2010

REFORM OF COUNCIL HOUSING FINANCE SYSTEM

1. PURPOSE OF REPORT

- 1.1 To advise on the implications of the consultation proposals on reform of the Council Housing finance system.
- 1.2 To outline the potential timescales and implications should the new Government proceed with the proposals.

2. RECOMMENDATIONS

- 2.1 That the Committee endorse the consultation response set out in Appendix A.
- 2.2 That further work is undertaken on the proposals in relation to the implications of the reform proposals, should they proceed, on the Mid Suffolk Integration and/or merger and on any future approaches to Stock Option Appraisal.

The Committee is able to resolve these matters.

3. FINANCIAL IMPLICATIONS

- 3.1 The new system will create additional financial capacity that can be invested in Affordable Housing and capital of repairs work to Babergh's existing housing stock.
- 3.2 It will also result in us retaining all of the capital receipts in relation to Council House sales as opposed to handing 75% over to the Government. This amounted to £0.6m in 2009/10.
- 3.3 Babergh's share of the debt settlement in relation to the proposals is £75m, which is considerably less than the £108m which would be paid to the Government in negative subsidy over the next 30 years.
- 3.4 This is a better financial arrangement than staying within the current unreformed system and the debt should be paid off in about 20 years time.
- 3.5 The proposals are likely to result in some revenue costs that are currently met by the Housing Revenue Account (the HRA) being transferred to the General Fund although these are expected to be relatively modest.
- 3.6 There could also be an impact on the General Fund Budget in relation to future capital financing costs. There appear to be options available, however, that would ensure the position is 'cost neutral'.

4. **RISK MANAGEMENT**

4.1 The report links most closely with the Council's Significant Business Risk No.10 – Local Response to National issues.

Risk Description	Likelihood	Seriousness or Impact	Mitigation Measures
The Government's proposals do not proceed or are amended to be less attractive leaving the HRA with limited funds in the future	Significant	Critical (in the longer-term)	Efficiency savings and effective prioritisation of revenue and capital resources as part of the 30 year HRA Business Plan.
Future interest rates and inflation costs rise, detrimentally impacting on the finances of the HRA.	Low	Critical	These should be manageable with effective Budget planning and Treasury Management. A 'safety net' mechanism in relation to the debt cap would be prudent to allow for unforeseen future costs.
Inability to transfer housing stock following a stock options appraisal.	High	Marginal	None.
Impact on Mid Suffolk integration/merger proposals.	Very Low	Marginal	Assess impact as part of detailed Business Case.
Potential costs to the General Fund	Significant (but low value)	Marginal	Review existing costs that are charged to the HRA and reflect any impacts through the SFP process

5. **EQALITIES AND DIVERSITIES**

5.1 It is envisaged that the proposals will not adversely impact on any Council House Tenants or other Babergh residents.

6. **KEY INFORMATION**

Background

6.1 The previous Government set proposals in train to dismantle the current unfair HRA subsidy system and replace it with a devolved self-financing system. These would remove the current position where the vast majority of Councils who are in "negative" subsidy (this effectively results in rents from tenants being handed over to the Exchequer - in Babergh's case, nearly £5m this year and growing year by year).

- 6.2 The proposed 'deal' is a voluntary offer to replace the current system in exchange for a one off redistribution of the national housing debt, with Council's retaining locally all future rental income and capital receipts.
- 6.3 It appears that the new coalition government remains supportive of the proposals and is not indicating this is an area of reform which will be scrapped. An announcement on whether the proposals are to proceed, on either a voluntary or compulsory basis and the timing, is expected in October.
- 6.4 We have commissioned external experts to analyse what the offer means for Babergh based on what we understand will be our share of the national housing debt. This external advice has been used to inform our draft response to the consultation, which was submitted by the due date of the 6th July 2010. Key aspects of the proposals were explained to the Housing Panel, the Political Leaders Group and at a Member briefing on the 14th July although attendance at the latter was disappointing. The Government has indicated that they welcome further responses beyond this official closing date.

The "Self-Financing" Proposal in Outline

- 6.5 Key elements of the proposed arrangements are set out below:

(a) End the current redistributive system in return for a one off settlement of debt.

- Babergh's debt settlement is £75m. This compares to the £108m which would be paid in negative subsidy over the next 30 years
- Taking on the debt is the price of reform. In simple terms, that is a better financial arrangement than staying within the current unreformed system. It should be paid off in about 20 years time
- If the current system remains, Babergh could have a £9m capital funding shortfall in 20 years time
- There could be an impact on the General Fund Budget in relation to future capital financing costs, although there appear to be options that are available that will be 'cost neutral'.

(b) The retention of a ring fenced HRA

- This would involve dismantling the current national HRA subsidy system but a separate "ring fenced" HRA would be retained to account for housing services that a landlord is required to provide
- This could result in some revenue costs that are currently met by the HRA being transferred to the General Fund. It is likely that the Government would proceed with this aspect, however, even if the overall proposals do not proceed.

(c) The retention of national rent policy

- We will still be required to follow the national rent restructuring policy under the proposals and would still be required to meet rent “convergence” to bring our rents in line with Registered Social Landlords to the national formula by 2015/16.

(d) The right to retain all capital receipts

- We would also retain all capital receipts from sale of housing and land that fall within the HRA, providing that 75% of those receipts are used for affordable housing & regeneration projects with the remaining 25% being available for any capital purposes (as now)
- This changes the current arrangements whereby 75% is paid over to the national pool.

(e) The self-financing settlement model & investment in council housing

- This is the biggest area of change and is based on a self-financing model taking into account income and spending needs and the calculation of a sustainable level of debt for each Council
- The model includes significant uplifts to the existing Management & Maintenance and Major Repairs Allowances giving every council a guaranteed 10% more money than they have under the current system
- In addition the discount rate used in valuing the present net value of the business is proposed to be 7% rather than the 6.5% discount rate typically used in housing transfer. The Government expects Councils to use this additional financial “headroom” (about £3m for Babergh) to deliver up to 10,000 new council homes each year nationally by 2014 when combined with access to Social Housing Grant through the Homes & Communities Agency. This is the same funding model used to develop new accommodation in partnership with Registered Providers
- The “offer” is the assumption that the new model and increased financial freedom would allow Councils to embark on a house building programme and/or increase spending on Council Housing regeneration, improvements or repairs
- Initial indications are that the benefits are quite significant in that we could use the extra money to build at least 125 new housing units over 5 years or increase repairs and capital expenditure by 25%.

Implementation Timescales

- 6.6 If there is consensus agreement amongst Councils, the Government may decide to work towards a voluntary implementation, potentially from April 2011, subject to confirmation at the next comprehensive Spending Review in October.

- 6.7 Further work would be required on our HRA Business Plan and related aspects if we were to look to be ready for that start date. It is likely that the work involved could be difficult to complete in such a short timescale.
- 6.8 Alternatively if there is not agreement the Government may seek to implement self-financing through new primary legislation and subject to parliamentary time and this would then not be before April 2012, either on a voluntary or potentially compulsory basis.

Summary

- 6.9. Officers believe that the proposals should be supported (subject to seeking certain clarification as set out in the draft response in Appendix A) as our external advisors indicate that we would see a fairly immediate gain under the new arrangements when compared to the current system.
- 6.10 The greater flexibility to determine our own spending priorities, in accordance with the views of our tenants and our 30 year business plan, is to be welcomed as is the greater autonomy which these proposals appear to provide and which free us up from central government control.
- 6.11 We also welcome the potential within the offer to embark on a house building programme on the same equal footing as Housing Associations who have always retained all the rents they collect. The Housing Panel will assess whether it is feasible for us to do so once we know the outcome of the consultation.
- 6.12 We need to be assured however, that the government will not be capable of reopening the debt and the circumstances in which these might be enacted. We also need greater clarity on some of the technical issues including a proposed cap on future debt, which could restrict investment in the medium to long-term.
- 6.13 In addition, clarification is sought from the Government that the proposals would not be an impediment to any merger with Mid Suffolk. Our consultant has given some initial thought to any specific implications and it does not immediately appear that there would be any significant issues. However, further consideration will be given to this.
- 6.14 Similarly, certainty and clarification on the impact of the proposals on stock option appraisals and the transfer of our housing stock to a Registered Provider. It appears that, as a result of the new share of debt exceeding the transfer value of the stock, there will be little prospect of any future transfers being viable. Of course, this will be less important in terms of investment in the housing stock as there will be much more financial freedom to run our own Council Housing affairs in future if the proposals go ahead. We will again consider the implications in more detail.

7. APPENDICES

A – Provisional Consultation Response.

8. **BACKGROUND PAPERS REFERRED TO:**

Consultant's report – HRA Reform Review.

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HRA Reform Proposals - Provisional Consultation Response

Dear Mr Edwards

Response to the consultation on Council Housing: A real future

I am pleased to confirm our provisional response to this important area of consultation. This matter will now be considered by our Strategy Committee on 29th July 2010 and if there are any further issues raised I will let you know. I will now summarise our initial responses to the questions raised.

1. What are your views on the proposed methodology for assessing income and spending needs under self-financing and for valuing each Council's business?

- We support the move to amend the Council Housing Finance system and the increased management and repairs allowances, as these assumed items of expenditure fall short of what we require and do not reflect the range of the services we actually deliver. However, we believe that there should be further consideration for an increase to these allowances to bring Councils in line with housing associations
- We need assurance from the Government that they will not reopen the overall settlement. We also seek clarity on whether the debt 'cap' can be extended in the future to sustain ongoing increases in investment, should this be affordable within Council's 30 year Business Plans
- We would strongly oppose the basis of the settlement if our proportion of the debt exceeded the overall debt that is currently in the system because this would make us more reliant on government support, which cannot be guaranteed in these difficult times
- We seek further clarity and certainty on future policy. For instance will rent convergence remain in its current form or are new legislative requirements likely to increase the level of spending within the HRA? If the formulas used to calculate the settlement are inaccurate or change over time, this could create the same uncertainty that exists with the current annual subsidy determinations and have undesirable impacts on our spending plans
- We also seek a detailed response on whether these proposals are intended to make large scale voluntary transfers of housing stock redundant. We are intending to commence a stock options appraisal at the end of the year and we must avoid making expensive commitments to this process or to raise the expectations of our tenants. Certainty from government on this matter would be helpful.

2. What are your views on the proposals for financial, regulatory and accounting framework for self-financing?

- We welcome the increased freedom on being able to spend all capital receipts locally
- We would like to see further detail on all the technical issues before commenting further. We believe such issues should be addressed within the implementation period to minimise the potential for any further delays
- We also believe that there should be no financial impact on the General Fund as a result of the proposals. If there are, we believe these should be funded by the Government.

3. How much new supply could this settlement enable you to deliver, if combined with social housing grant?

- Our initial forecasts indicate that we could deliver 175 new homes over the next five years (*to be amended to 'at least 125 new homes*). We will however, be seeking further clarification as to whether local targets will be set and whether the debt cap will be abolished to give us greater flexibility to deliver new homes, should we receive approvals to do so, within the duration of the agreement.

4. Do you favour a self-financing system for council housing or the continuation of a nationally redistributive system?

- We believe that the current system is unfair and insensitive to our plans to deliver effective outcomes for local people and therefore we support, subject to the caveats outlined elsewhere, the dismantling of the current subsidy system on the basis of a fair and viable one- off settlement which allows us to manage our future finances at a local level.

5. Would you wish to proceed to early implantation of self-financing on the basis of the methodology and principles proposed in this document? Would you be ready to move to self-financing in 2011/12? If not, how much time do you think is required for implementation?

- We have already stated that we favour self-financing as an alternative to remaining within the subsidy system. However, some aspects require clarification, including the precise nature of the new agreement between the Government and Councils and the revised accounting arrangements to ensure these are as simple, clear and transparent as possible. These are a real failure of the current system
- Subject to the above, we would be keen to move to self-financing from April 2011 if that were possible. This means that the Government needs to make the earliest possible decision on proceeding. We cannot wait until the Comprehensive Spending Review in October
- We also seek assurances that the Public Work Loan Board will have the capacity to fund the debt under the new system as up to 170 Councils may all move to the new arrangements at the same time
- However, that should there be any delays to the plans which are unavoidable, that the government consider making transitional arrangements to our negative subsidy arrangements in 2011/12.

6. If you favour self-financing but you do not wish to proceed on the basis of the proposals in this document, what are your reasons?

- We favour the proposals to move to a new system, subject to there being further clarity and understanding of the issues we have raised

And finally, we are in advanced discussions with our neighboring Authority, Mid Suffolk, about service integration and constitutional merger. I ask you to note these intentions and hope that nothing contained within these proposals will act as an impediment to the plans taking effect.