Report for Information

Report to	Executive 23 June 2010	6
Report of	Head of Finance	
Subject	Housing Revenue Account proposal consultation	

Purpose

To inform members the principles of the housing revenue account (HRA) prospectus consultation, describe the evaluation of the proposal, and recommend a response.

Recommendations

That the Executive:

1. Agree or amend the draft response to the consultation proposal (to be tabled at the meeting)

2. Delegate to the Chief Executive, in conjunction with the Portfolio Holder, any amendments arising from the meeting of the Scrutiny Committee.

Financial Consequences

The financial consequences of this report are described in the body of the report.

Risk Assessment

The risks attached to the proposals are described in the body of the report.

Strategic Priority and Outcome/Service Priorities

The report is relevant to the strategic priority “Safe and healthy neighbourhoods – working in partnership with residents to create neighbourhoods where people feel secure, where the streets are clean and well maintained, where there is good quality housing and local amenities and where there are active local communities” and a number of service plan priorities concerning the creation, maintenance and improvement of council homes.

Executive Member: Councillor Arthur - Housing and Adult Services

Ward: University

Contact Officers

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Background Documents (available from contact officers)

CLG Consultation papers
HRA Business Plan Model
Working papers

Report

Introduction

1. Following too many months of discussion and consultation, the previous government asked councils to indicate whether they wished to have the freedom fund and run their council houses without annual government decisions over subsidy. To achieve this the government have made a proposal to every Local Authority (LA) with retained stock (177 in total) an offer to take on a specified portion of the national housing debt in return for leaving the existing housing subsidy system. This would mean that interest and debt repayments will replace current negative subsidy payments. The Government are seeking consultation on this proposal.

2. Currently responses to consultation are required by 6th July as to whether council's wishing to accept this proposal via response to six questions. (See appendix 1). It was presumed that the government would then examine the responses and decide whether to enter voluntary agreements to leave the HRA with individual authorities.

3. Prior to the recent general election indications were that three all main parties supported the proposal in principle but any final decisions would be subject to spending reviews.

The existing Housing Subsidy system

4. The Subsidy system was designed to redistribute council housing resources nationally, so that each council would be funded to provide management, services, repairs, and investment irrespective of its actual rent income.

5. To achieve this, councils surrender their rent income to CLG through a mechanism known as Guideline Rent, and receive in return allowances for Management & Maintenance, Major Repairs, and Capital Charges (borrowing costs).

6. The current cost to Norwich of the subsidy system is shown below:

Management & Maintenance Allowances	£27.1m
Major Repairs Allowance	£9.8m
Capital Financing (debt interest)	£6.7m
Guideline Rent	(49.5m)
Other	£0.1m
Total Negative Subsidy (paid to government)	**(£5.9m)**

7. The system is complex and lacks transparency, can be volatile from year to year, and has been described by the Audit Commission as no longer fit-for-purpose.

8. The system is currently failing to redistribute council housing resources fully, and large undistributed surpluses are expected to accumulate in future years.

9. For these reasons, the government is consulting on its abolition and replacement

by a “self-financing” system which addresses these shortcomings.

10. The proposed replacement self-financing arrangements comprise a one-off redistribution and allocation of housing debt instead of the current annual redistribution of income and expenditure allowances.

Allocation of Debt

11. Total debt to be allocated is £25.13bn, i.e., an additional £3.65bn over and above the existing housing debt. Communities and Local Government (CLG) has provided the financial model used to calculate the level of debt to be allocated to each local authority. CLG intend that this should also thereafter be the maximum borrowing allowed.

12. The intention is that the amount of allocated debt would be at a sustainable level (i.e., affordable within each Local Authorities’ (LA) HRA) and therefore the assumptions used within the debt allocation model and the implications of the starting debt figure for each council’s housing revenue account business plan need to be considered very carefully.

13. Technically, the model is based on a net present value calculation of notional expenditure and income assumptions with annual cash flows discounted back to a 2011/12 price base. The key figure is the discount rate which will determine the level of debt and how long it will take to repay. Where a council’s debt allocation is greater than their subsidy capital financing requirement they will be required to make a payment to Communities and Local Government (CLG) and where the debt allocation is less they will receive a payment.

Rent levels

14. Income within the self financing model is based solely on rents, with the stated assumption that actual rents will converge with formula rents by 2015/16. Adherence to government rent policy will be secured by the continuation of limit rents and Tenant Services Authority regulation (TSA).

15. The proceeds of future rent increases (the excess of RPI-inflated income over inflated expenditure) would benefit LAs rather than resulting in increased negative subsidy as at present.

New build

16. The total debt allocation of £25.13bn is based on the use of a 7% discount rate within the debt allocation model. CLG state that this is being used instead of 6.5% in order to free an additional £1.2bn which should fund 10,000 additional new build properties per year by the end of the next parliament - at the time of writing this was presumed to be five years. The consultation is seeking confirmation from councils regarding the size of new affordable homes programmes which could be supported.

17. For Norwich, a £9m difference between the two discount rates shows the additional investment funding that would be available for new build. The capital and revenue impacts of this are assessed within the HRA Business Plan model.

Repair and improvement of the stock

18. The government has identified that there is an outstanding requirement of £3.2bn for spend on decent homes works; funding for these works would be part of the future spending review process. Notional expenditure is based on projected subsidy allowances. The average MRA uplift is 27% rather than the 24% proposed by the BRE. Overall the average combined MRA and M&M uplift is 11% with just 27 councils getting less than 10% and eight getting more than 14%.

Right to buy and sale of land receipts

19. Currently, councils are obliged to pay 75% of RTB receipts to the government.

20. As part of the self-financing proposals, pooling of capital receipts will end and authorities will be able to retain their HRA capital receipts - provided 75% of these have been or will be used for affordable housing and regeneration projects. The remaining 25% may be used for any capital purpose.

What tenants should be paying for and not be paying for

21. The consultation includes revised guidance on the HRA ring-fence with a set of principles for deciding whether a service should be paid for through the HRA or the General Fund.

22. This guidance is largely a restatement of existing ODPM/CLG guidance, and will help to demonstrate that the interests of tenants and non-tenant residents are being equitably

What self-financing would mean for Norwich

23. The Management & Maintenance allowances would increase by 4.8% (national average 5.4%) and Major Repairs Allowance by 2.95% (national average 28.2%). These are notional amounts which reflect the “need to spend” and therefore reduce the debt settlement.

24. The debt figure for Norwich would be £213m at the 6.5% discount rate (excluding allowance for new build) or £204m at the 7% discount rate (including allowance for new build). This would be an increase of £132m (6.5%) or £123m (7%). The self financing model indicates that the debt is sustainable, in that it can be paid off from the HRA within 25 years (6.5%) or 23 years (7%).

25. Because our current HRA borrowing is less than the assumed borrowing in the self-financing model, our actual borrowing would increase to lower totals of £187m (6.5%) or £178m (7%).

26. The £9m difference between the two figures shows the additional investment funding that would be available for new build. Options for use of this resource are explored in the evaluation of the offer.

27. The evaluation will also consider potential application of financial benefits, e.g., in the possibility of delivering an investment programme at a higher level than the minimum Decent Homes standard currently planned.

Risks

28. The largest risk to the Council is that the debt settlement would be less beneficial than the continuation of the existing Subsidy system. Early work on modelling the impact shows that the settlement would be beneficial, and this risk is therefore minimal.

29. A secondary risk is that better terms for a settlement could be obtained, i.e., lower additional debt. Feedback from our consultants, other professionals, and inferences drawn from the state of the national economy point to a strong likelihood that any alternative terms would be less beneficial.

30. A tertiary risk is that the new government may review the terms offered in the prospectus issued under the old government, and make a less beneficial offer. The impact of lower discount rates (and therefore higher debt settlements) will be modelled to evaluate the reduction in financial benefit that would follow.

31. There are longer term risks arising from acceptance of the settlement, in that the Council would need to manage its housing stock and services within its own resources. The prospectus makes it clear that central government would remove itself from the management and resourcing of council housing, other than by regulation through the TSA.

32. Other risks include the treasury management consequences of the additional debt, increased exposure to interest rate fluctuations and inflationary increases, and adverse price changes in future repair & improvement contracting.

Evaluating the offer

33. External support has been procured from ConsultCIH and work undertaken on the detailed analysis of the proposed settlement for Norwich.

34. A consultation event for tenant and leaseholder representatives has been arranged for 16 June.

35. The debt allocation is based on notional expenditure and income, and the performance of the HRA business plan will depend on the relationship between actual management, maintenance and major repairs costs and rent income and the assumptions. The government has provided a financial model and it is expected ‘’councils to test the opening debt figure proposed under self financing in a local business plan which reflects local information about actual income and expenditure and borrowing costs.” This involves various scenarios and tests for sensitivity and risk. Options for use of the new build resources are also explored.

36. Officers have examined in detail through a Business Plan model what the offer means for Norwich and have sought specialist advice from ConsultCIH. This advice is attached as Appendix 2 to the report.

37. Recommended responses to the consultation questions will be drafted for the Executive’s consideration based upon the specialist advice and on the result of consultation with stakeholders. A draft response will be tabled at the meeting of the Executive.

38. Scrutiny Committee will consider the Executive’s decision at its meeting of 24

June. It is recommended that the Chief Executive, in conjunction with the Portfolio Holder, is delegated the authority to amend the draft responses in the light of Scrutiny's deliberations.

39. The government will then examine the responses and decide whether to proceed on a voluntary basis with the offer on these terms, or to proceed on some other basis.

Evaluation

40. The principle criterion against which the offer has been evaluated is whether tenants interests are better served under self-financing than under the existing subsidy system

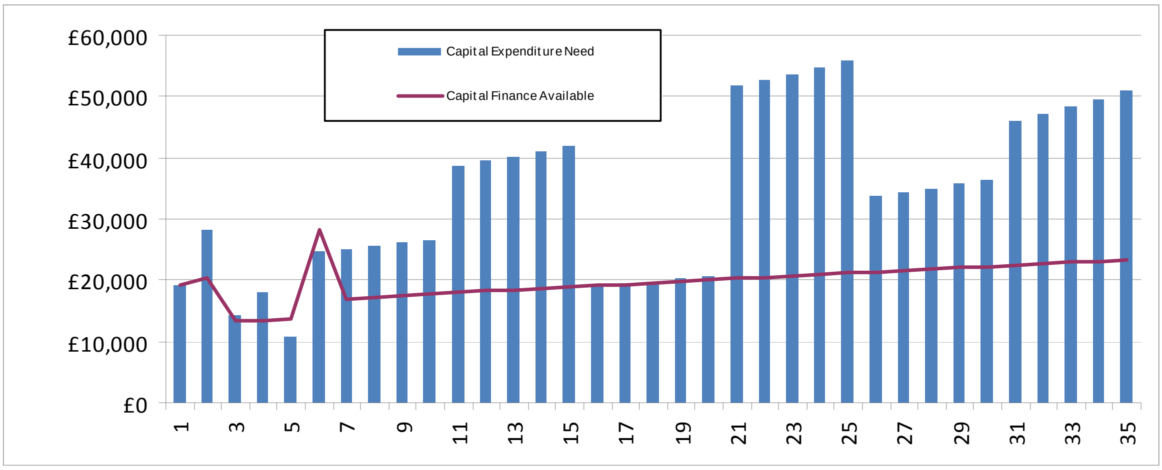
41. In order to demonstrate this, self-financing needs to demonstrate:

- That risks under self-financing are manageable if greater than under subsidy;
- That more resources are made available for the provision of management and repairs, and for capital investment in the housing stock
- That the Housing Revenue Account remains financially viable (i.e., does not go into deficit) over the long term planning period.

42. The consultants' report attached as Appendix 2 indicates that these tests are clearly passed by the self-financing offer under current external circumstances (e.g., inflation rates, interest rates) and to a lesser (though still adequate) extent if there are adverse external factors.

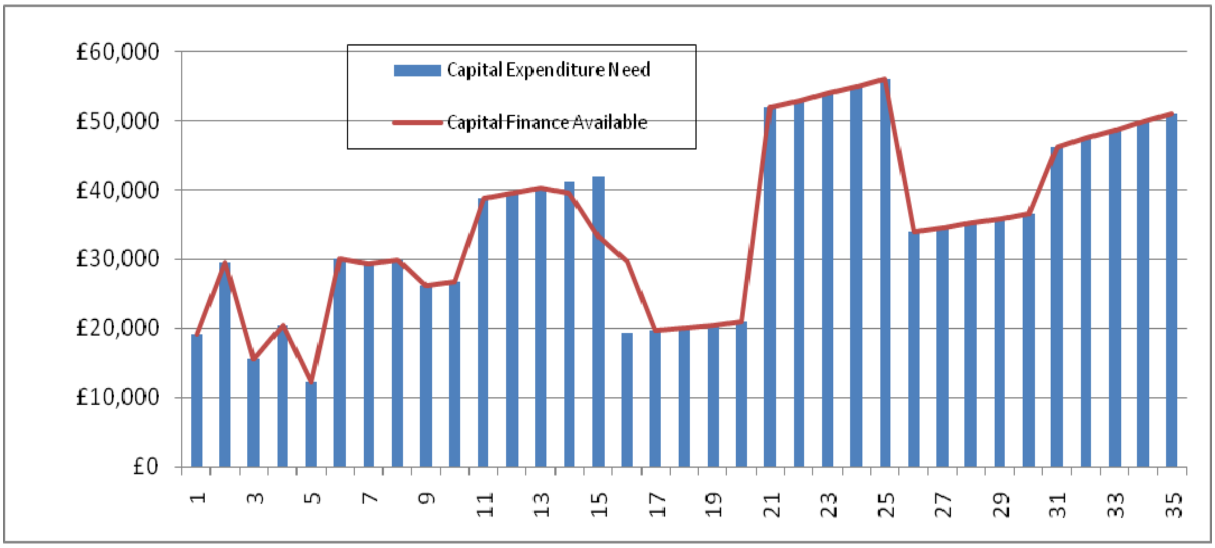
43. This can be most clearly shown by comparison of the investment in major repairs and improvements affordable under the existing subsidy system with these affordable under self-financing.

44. Under the existing subsidy system, where the need to spend on a sustainable and fully "Decent Homes" investment plan is shown by vertical bars and the availability of resources by the line, the position is:



45. This shows that the desirable level of investment cannot be provided from resources within the subsidy system. Modelling shows that the level of investment would need to be cut back by about 35% (i.e., to the current minimum Decent Homes standard only) to maintain an affordable programme.

46. Under self-financing, the same level of investment matched against funding capacity shows:



47. This indicates that self-financing can deliver sufficient resources to support the higher level of investment, with some re-profiling of spend mid-term. Additionally, in time revenue reserves can also be built up under the self-financing model.

Recommendation

48. Accordingly, the recommendation of this report is that the Executive agree the proposed draft response to the consultation (to be tabled at the meeting) and to delegate to the Chief Executive in conjunction with the Portfolio Holder any amendments arising from Scrutiny Committee.

Appendix 1

The six questions the government is requesting a response to.

The government has asked for a response from councils by 6th July 2010 as to whether they wish to accept this offer via response to six questions detailed below. It is anticipated the response will need to a detailed document as opposed to six yes or no responses

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?

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

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

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

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

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

It is assumed that each council will consider in detail what the offer means for them and decide whether it is acceptable or not. It is also assumed that councils will consult with key stakeholders, i.e., residents and members.

Appendix 2

Norwich City Council
Council Housing: a real future
Briefing on the implications of the HRA reform prospectus

1. Introduction

1.1 CLG published its long awaited voluntary 'offer' to local authority landlords on 25th March. The offer is in the form of a prospectus setting out the terms within which the government plans to implement the dismantling of the Housing Revenue Account (HRA) subsidy system and introduce a system of self financing from April 2011 on a voluntary basis.

1.2 Work has been carried out to model the impact of the reform proposals for Norwich City Council. This note sets out the main findings of the modelling work, highlights the main Norwich-specific issues to arise and provides a summary commentary on the proposals within the prospectus, with the aim of informing the council's response to the consultation, which is due by 6th July.

1.3 It is intended that officers will arrange for briefings to all stakeholders in order to discuss the issues raised in this paper as part of the Council's process of generating its response and we look forward to participation as requested in due course.

2. The HRA Prospectus

2.1 The reform proposal has been produced following the Review of Council Housing Finance which concluded in the summer of 2009 and following last autumn's consultation.

2.2 The proposal is based on moving towards a 'self financing' HRA system in which negative or positive subsidy is exchanged for a single one-off adjustment of housing debt following which rental surpluses and Right to Buy receipts are retained 100% by local authorities.

2.3 The allocation of debt is the Net Present Value[1] of a cashflow estimate of rents and revenue costs for all authorities over 30 years, based on subsidy rent assumptions which achieve convergence with targets by 2016 and subsidy allowance assumptions which include an uplift of funding. By linking the debt allocation to current and future subsidy assumptions, the government is making the settlement 'neutral' in national expenditure terms.

<u>The National Picture</u>

[1] Net Present Value or NPV: a financial technique to calculate the value of a future income stream (eg for a business) and convert it into a single amount at today's prices

2.4 Nationally, the total value of future rental surpluses in an unreformed system is estimated to be £34-35bn. Current debt is £21.5bn (forecast at 31st March 2011). Therefore the value of future surpluses is in the region of £13-14bn.

2.5 The total proposed allocation of debt is £25.1bn based on increased allowances of 5% for management and maintenance (M&M) and 28% for major repairs, with a discount factor[2] of 7%. This means that the government could be said to be capturing £3.6bn of surpluses up front and allowing all future surpluses to remain in local HRAs.

2.6 The prospectus identifies that the discount factor for recent stock transfers is lower at 6.5% - which applied to this settlement would result in a debt allocation of £26.3bn. The difference of £1.2bn is therefore treated as 'reduced debt' and there is an explicit reference to authorities setting out some ideas as to how to utilise the headroom from this debt 'reduction' towards new build. Nationally, the prospectus refers to '10,000 properties per year in five years'; although it is not clear how this figure has been developed, authorities are encouraged to set out some outline options in their responses.

2.7 From a revenue perspective, although higher than current debt, the proposed debt allocation is lower than might have been expected following the consultation period last autumn. At a national level, the distribution of increased allowances through the debt mechanism represents an increase in spending power for council housing that is not in line with public expenditure pressures elsewhere. This highlights that the proposal is a 'deal', in which government takes surpluses up front in order to reduce debt elsewhere in the public sector.

2.8 Where the proposals do reflect the significant spending pressures in the economy as a whole is on capital investment and borrowing. The new system would see supported borrowing replaced with a system of capital grants and the ability for HRA business plans to use prudential borrowing on a long term basis.

2.9 Research for last year's consultation identified outstanding backlogs for decent homes and other investment at around £6bn. The prospectus has cut back on this, focusing on the completion of decent homes mainly for later-round ALMO authorities. A figure of £3bn for capital grants is referred, although this would be subject to future spending reviews.

2.10 In addition to the level and uncertainty around the availability of future capital grants, the proposals also act to restrict future borrowing. Although the government has rejected the idea of setting borrowing limits annually, the prospectus contains an absolute restriction on future borrowing above the level of the initial allocation of debt. It is expected that this cap will last until at least into the spending review period after next (i.e. till after 2014).

[2] Discount factors in NPV calculations represent the time value of money: in this case, the discount factor represents an assumed level of interest costs.

2.11 Effectively, therefore, self financing HRA plans will need to be based largely on revenue and receipts with reliance on borrowing restricted to any existing gap between actual debt and supported debt. Most authorities are unlikely to be in a position to receive grants. The settlement might therefore be said to be '*Revenue-Positive*' and '*Capital-Challenging*'.

2.12 There are a host of technicalities associated with the implementation of the new arrangements, including a proposal to report a memorandum HRA balance sheet and various options for the treatment of depreciation, debt repayment and treasury management. Where relevant for Norwich, these are highlighted below.

2.13 The proposals are intended to be a 'once and for all' settlement. A self financing agreement would be signed under clause 313 of the Housing and Regeneration Act 2008. However, as council housing will continue to be 'on balance sheet' for public expenditure purposes, the government will retain the right to 'open up' settlements in the future. The circumstances in which this might take place are not set out and it is essential that self financing agreements are very clear about these circumstances. One obvious example is change to future rent policies i.e. if rents increase higher or lower than assumed in the settlement, the debt calculation might be reopened.

3. Norwich's modelling: main assumptions

3.1 A model has been produced for Norwich launched from 2010/11 and based on the existing budget and 5 year capital programme, with the following key assumptions:

- Balanced to 2010/11 HRA budget and 2010/11 capital programme
- Rents converge (with similar housing provider properties) in 2015/16 (with no property-by-property adjustment for caps and limits[3])
- Roll forward of management and maintenance expenditure with inflation (i.e. no real terms investment or efficiencies)
- Roll forward of non-rent income with inflation
- Right to Buys of 50 per annum
- General inflation (RPI) of 2.5%
- Long term debt interest rates of 6% (early years in line with current rates)

3.2 A critical assumption relates to the stock investment and capital needs for the stock over the longer term. These have been factored into the business plan based on the asset management system and data the Council holds, which has been updated by officers. The 30 year capital profile amounts to around £45.1k/unit and this is above similar benchmarks, though reflects some of the construction types of properties within Norwich.

3.3 The modelling provides a headline sense of the viability of self financing given the debt settlement and no access to capital grants. The plan is

[3] Caps and Limits refer to restrictions on individual rent increases of RPI plus 0.5% plus 2% and not breaching a set rent (for housing benefit purposes) for a property, dependant on the number of bedrooms

developed in two core scenarios: one with debt maintained and one with revenue surpluses set aside to repay debt.

4. Proposed settlement for Norwich

4.1 The headline debt settlement from CLG for Norwich amounts to £203.780m. This is based on uplifted M&M allowances of 4.9%, uplifted MRA of 29.5%, resulting in a consolidated average uplift of 11.4%.

4.2 Norwich's M&M increase is larger than for the rest of the Eastern region's average of 2.6% and is lower than the national average due to the lower percentage of flats in Norwich, particularly high-rise. The MRA uplift is higher than the national average but lower than the region's 31%.

4.3 The £203.780m settlement is based on a 7% discount factor. A reduced discount factor of 6.5% would give a settlement of £213.322m, a difference of £9.542m. The prospectus asks authorities to outline suggestions for how they might use this 'headroom' to deliver more housing. No new build has been included in the plans below but scope exists given the outputs to develop plans.

4.4 Given a settlement of £203.780m, the debt adjustment for Norwich is £122.900m which is arrived at by offsetting the existing HRA 'notional' debt SubsidyCFR[4] of £80.880m. This results in an 'opening self financing debt at 1/4/2011' of £181.377m when added the actual HRA debt (HRACFR[4]) of £58.477m. The existing differential between subsidy-debt (Subsidy CFR) and actual debt (HRACFR) of £22.403m is therefore retained as borrowing potential within the new system for Norwich.

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5. Headline outputs

5.1 The headline outputs for two core approaches to self financing are set out below. The CLG debt profile is shown for comparative purposes. These are (i) the maintenance of debt with continued refinancing (i.e. only paying interest) and (ii) the repayment of debt from future surpluses.

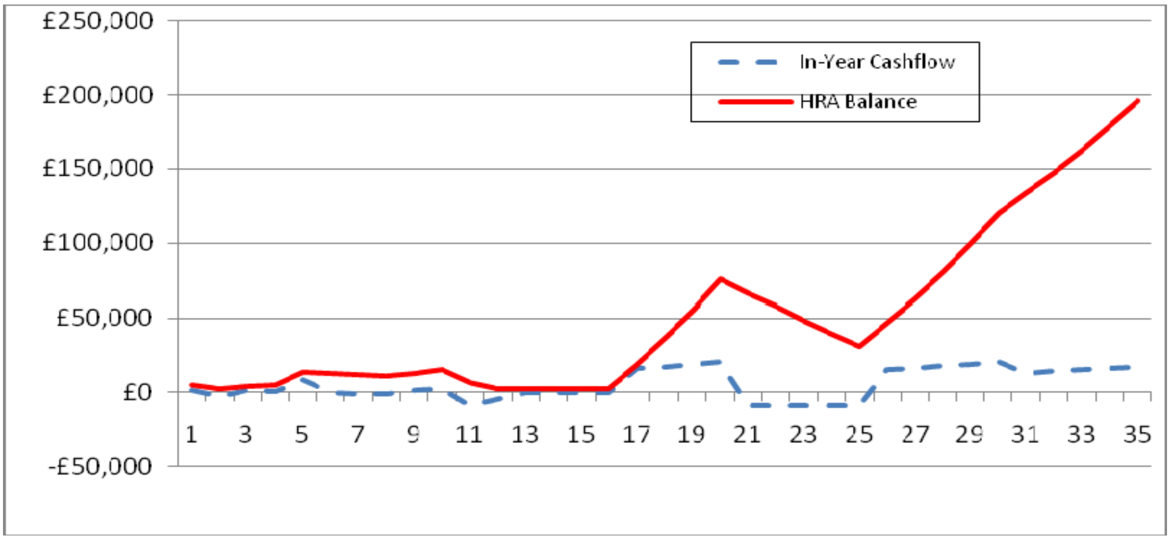
5.2 This shows that both plans are financially viable and meet all expenditure needs in each year of the 35 years covered by the plans. There is some borrowing required throughout to meet the stock investment needs over the length of the plan.

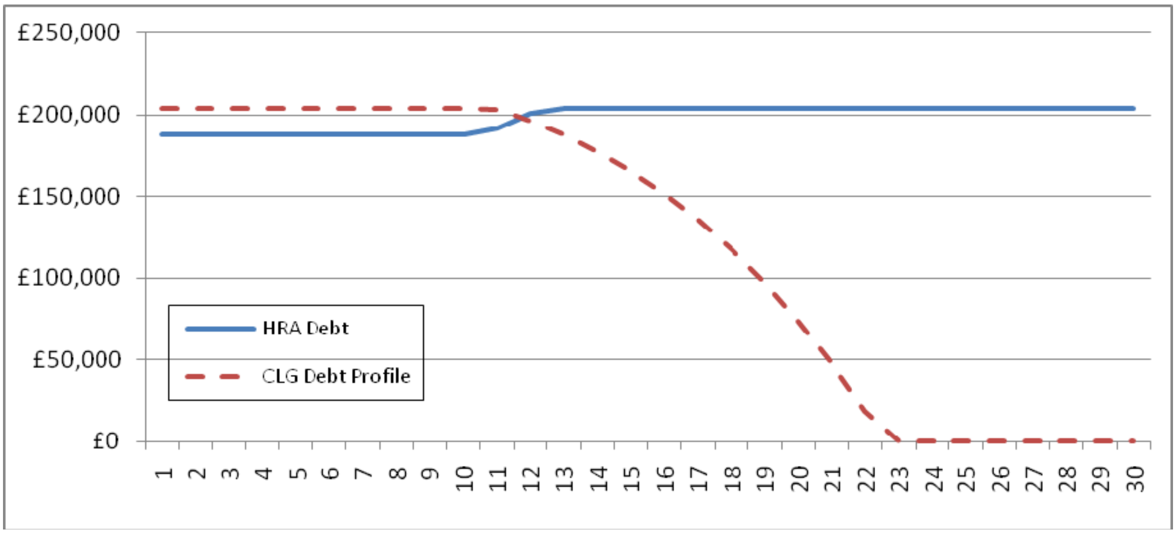
5.3 If debt is maintained as in (i) at £181.377m, reserves build to above £196m after 35 years. Charts 1a and 1b show the outcome.

5.4 If revenue surpluses are set aside to repay debt, repayment can be achieved after 30 years (compared to the CLG's assumption of 23 years) and reserves also built to nearly £105m after 35 years. Charts 2a and 2b show the outcome.

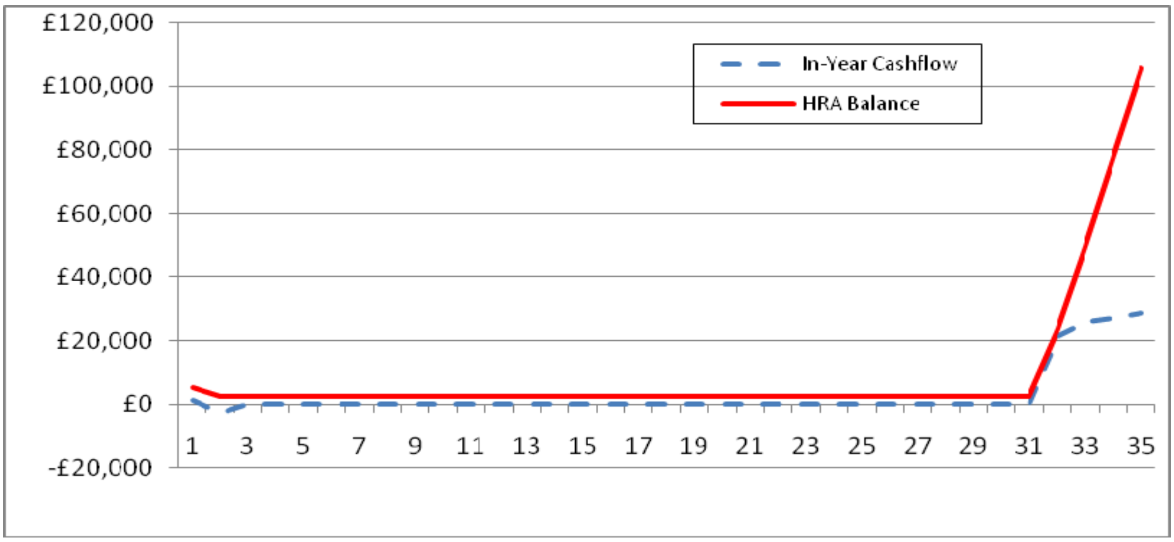
[4] The HRACFR is the actual element of the council's overall surplus or debt relating specifically to Housing. The SubsidyCFR is the assumed level of surplus or debt within the current subsidy system for the council's HRA.

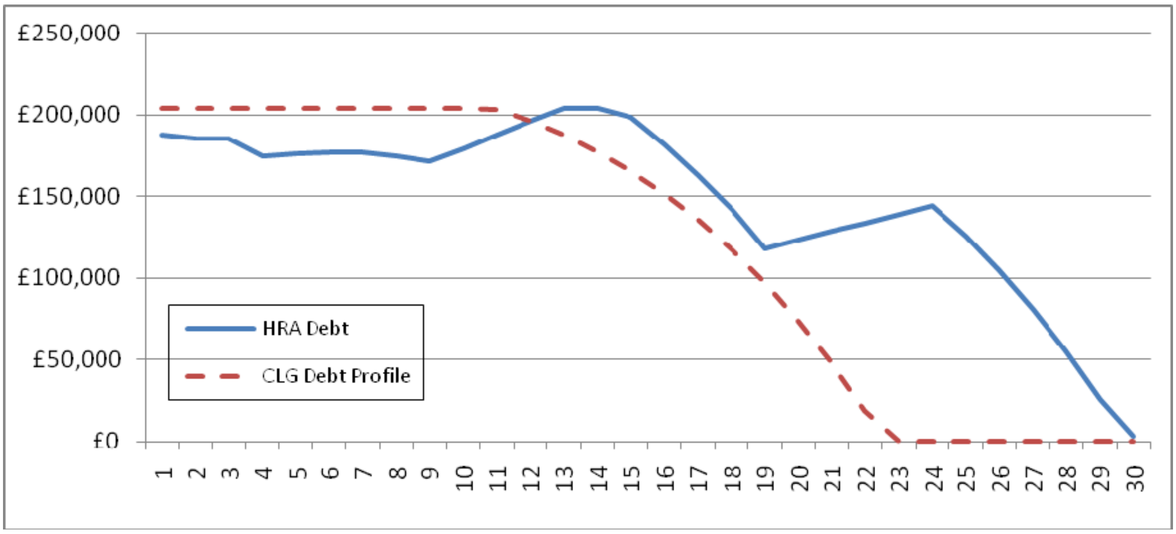
Charts 1a and 1b: Self financing revenue and debt profiles £'000: no set aside





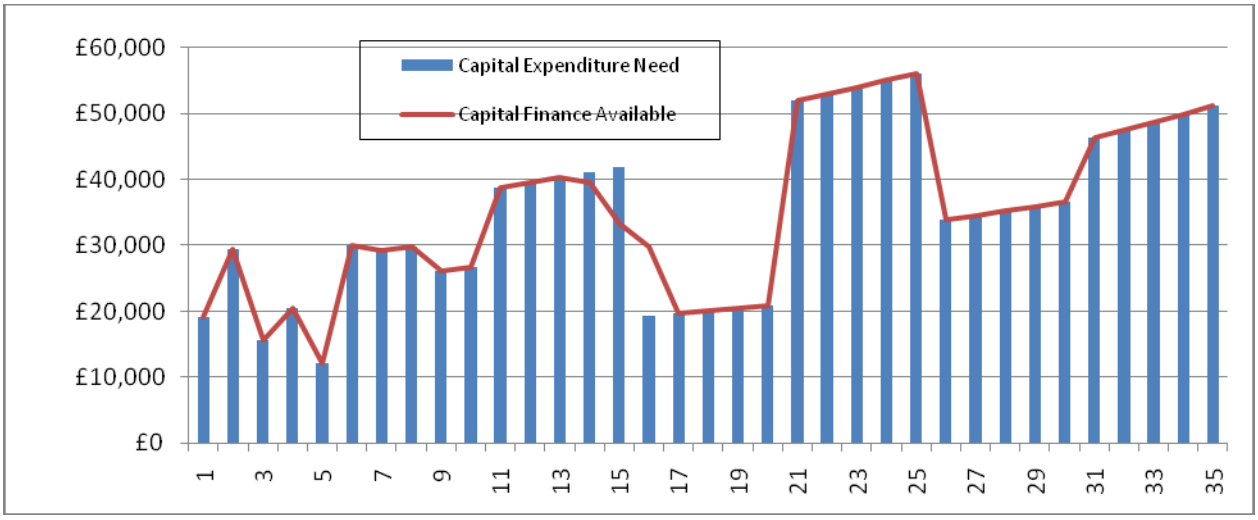
Charts 2a and 2b: Self financing revenue and debt profiles with set aside £'000





The Council's assessed capital investment needs, based on property surveys, are able to be met, with the exception of one year, in the plan. With re-profiling of expenditure this can easily be met. Chart 3 highlights the position.

Chart 3: Capital expenditure needs against resources annually £'000



6. Sensitivities

6.1 The plan is viable but not resilient to changes in key assumptions. Some key headlines are set out below.

6.2 If interest rates were 8% not 7%, the debt repayment plan redeems debt beyond year 35 (compared to year 35). Overall the plan remains viable with minimum reserves at year 35.

6.3 Real inflation in capital costs (1% pa for 10 years) results with debt repayment pushed out beyond year 35. Overall the plan remains viable with minimum reserves at year 35.

6.4 Real inflation in management and maintenance costs (additional 1% pa for 10 years) reduces revenue surpluses but results in the plan remaining viable with minimum reserves at year 35and debt repaid beyond year 35.

6.5 If rent convergence was unable to be achieved until 2022 (say), this also has the effect of reducing revenue surpluses but debt repayment would be achieved beyond year 35.

6.6 The modelling above assumes all of the income from right to buy receipts and is therefore susceptible should sale levels fall below 50 per annum.

7. Summary of modelling outcomes

7.1 In general, self financing based on a debt adjustment of £122.900m is viable for Norwich.

7.2 The principle reasons for the positive model for Norwich are:

- Rents are £7.61 below target[5] in 2010/11 hence the self financing plan builds headroom against current operating costs quickly in the period to convergence.
- Net forecast actual M&M costs in 2011/12 are £24.37m, after service charge income and non-dwelling rents, higher compared to assumed M&M (after uplifts) in the settlement of £29.30m.
- Debt begins some £22.4m below settlement – this allows the necessary borrowing to be undertaken to meet needs in the early years.
- The HRA and Major Repairs Reserve have combined balances of £6.4m

7.3 This means that although capital spending needs are £45.1k/unit over 30 years compared to uplifted MRA/unit of £24.8k/unit, there is sufficient headroom in the plan to achieve all the capital needs, subject to the sensitivities above.

8. Comparing self financing to subsidy

8.1 Self financing business plans on the basis of the current proposals are almost universally better funded than plans based on an unreformed subsidy system. This is the case for Norwich and principally arises as a result of the following key factors:

- The benefits of all net rent increases are available to the plan – i.e. surpluses are not captured nationally and redistributed; this is the critical difference between the two futures as rental surpluses are expected to be rise sharply in the future.
- The allocation of uplifts for M&M and major repairs allowances gives additional spending power from day one.
- The interest charge on debt is at the same rate as the discount factor used in the settlement calculation.

[5] Target or Formula rent is the level of rent attributed under rent restructuring and is the level of rent to which actual will eventually converge to. Other housing providers rents have to abide by this system.

- The opening debt is lower than that identified in the settlement (due to the difference between the CFR measures).

8.2 In an unreformed system, the following are the main comparative outputs:

- Instead of fully funding the above capital needs, there is a capital shortfall over 30 years estimated at £508m out of a total spend of £987m (including inflation). The shortfall starts occurring after 2 years. This is based on the full investment standard. If the level of capital expenditure was reduced to the minimum decent homes standard, the expenditure could be met but is reduced by 35% to £27.2k per unit of £579m total spend.
- The forecast HRA position is broadly in balance for all years of the plan in either of the above scenarios in the unreformed system.

9. Technical issues for Norwich

9.1 There are a number of technical issues which are still to be resolved at the national level. These include the treatment of depreciation and the approach to the separation of debt between the General Fund and HRA.

9.2 For Norwich, as for others, there is a need to generate a fair depreciation charge for the HRA and this will no longer benefit from a link to the MRA as with the current system. Councils are advised to work through the options in advance of work to be undertaken by CIPFA and the Audit Commission which is expected to be completed later in the year,

9.3 As the council is taking debt on, there are some options in terms of Treasury Management (for example long term fixed rate loans vs variable rate loans). It should be noted that the government has expressed a desire to move to a greater GF/HRA separation of debt and the council should work through the implications carefully.

9.4 Furthermore as the General Fund currently benefits from the average overall CFR, with the HRA taking on debt, it is expected that the Consolidated Rate of Interest (CRI[6]) charged to the General fund could increase. However the consultation suggests that local decisions could be made as to the allocation of debt, if the debt is separated and this should not be to the detriment of the General Fund.

9.5 Revised draft guidance on the operation of the HRA ring fence is included in the prospectus carrying with it some proposals around the treatment of certain types of expenditure. Councils are advised to work through whether this might create movements between the accounts to inform their response.

10. Risk and reward

10.1 Moving to a self financing system significantly alters the risk profile in HRA business plans and the council housing service.

[6] The CRI is the average rate of interest across the Councils debt or retained surpluses.

10.2 The risks of the current system focus on unpredictability and political intervention in the system (in the widest sense) and on the fact that revenue rental surpluses will leave Norwich to other parts of the country.

10.3 New risks are around increased Treasury Management, interest rate fluctuations and the fact that the council will have local responsibility for all spending (revenue and capital).

10.4 A robust risk management strategy is therefore an essential strategic document to support the asset management decisions within the business plan.

11. New Build

11.1 Contained within the announcement of this "offer" was a statement that by reducing the level of debt council's will be taking on they should be able to deliver 10,000 new homes a year. At this stage we are not certain as to whether council's debt settlements are dependent on the ability for you to deliver new homes within the HRA.

11.2 What could this mean in terms of delivery of new properties? We have interpreted this in two ways assuming build costs of £100k per unit at a high level:

11.3 <u>Example 1</u>
At 6% CRI the debt charge 'saved' are £573k per annum. Over 5 years this, combined with 50% grant could deliver nearly 57 properties, or 286 over 30 years.

There will obviously be benefits to the HRA of rental income from these properties, though these will be offset by management, maintenance and improvement costs.

11.4 <u>Example 2</u>
Further accurate modelling can be undertaken within the business plan model once more accurate knowledge around land availability, build costs and property types are known to help inform the response to CLG.

However by assuming build costs of £100,000, grant of 50%, rents of £67 and assumed levels of repairs and maintenance we estimate that 150 properties could be provided for in the first 5 years. This analysis that taking account all income, expenditure and notional interest, the new build schemes would break-even over 30 years. When applying these schemes to the actual HRA Business plan, the debt repayment is extended by one year.

12. Summary national issues

12.1 The large majority of authorities, like Norwich, will have a potentially viable plan and certainly one which has more resources compared to staying in an unreformed system. In this context, the overwhelming majority of authorities may well be minded to respond positively to the proposals for self financing on the terms that they appear in the prospectus. However, there are some national caveats.

12.2 Given that the prospectus has been issued at a time of considerable change with financial and policy uncertainty, there is the potential for the proposals not to proceed to implementation as planned. Three areas felt to be key are:

- The number and type of authorities that say ‘no’ to the proposals or are not in a position to respond positively – it is unclear whether CLG have a number in mind that might affect the future for those that do want to proceed.
- The outcome of the General Election and the policy uncertainty that this brings.
- The financial terms of the proposals will be subject to a Spending Review (or equivalent) in the autumn which might affect some of the assumptions.

12.3 Given the direction of travel of the recent political debate, it may be that the methodology within the settlement remains essentially intact but that there is a risk that the financial terms are affected by very close scrutiny by new policy makers.

13. Summary of Implications to Norwich

13.1 These are the key conclusions from our analysis of the implications to Norwich:

- The settlement of £203.78m results in a net debt take-on of £122.900m.
- The uplifts to the allowances to arrive at this figure are generally marginally lower when compared with the region and national averages
- The resulting take-on of debt and withdrawal from the subsidy system result in revenue surpluses to finance the resulting interest charges and facilitate debt repayment
- Norwich could repay the debt repayment within 30 years, though various factors could extend this period.
- The HRA will remain viable throughout this period with balances accruing after debt repayment.
- The Council’s assessment of its stock investment needs can be fully met throughout the duration of the 35 year plan.
- The key reasons for the viability and resilience to changes in assumptions is that plan starts with balances in reserves, interest rates that can outperform those allowed for in the settlement.
- The financial position under self-financing is significantly improved compared to remaining within subsidy.
- The settlement offers the potential for HRA new build.

14. Summary of Key Issues for Norwich in responding to the prospectus

14.1 These are the key issues Norwich should focus upon in their response to the prospectus:

- Questions could be raised in respect of the uplifts to allowances to arrive at the settlement, when making comparisons to neighbouring authorities.
- Clarification needs to be made around the ability to reopen debt and the circumstances that this would be enacted.
- With regard to HRA new build levels, clarification should be sort as to whether local targets might be set and the duration.

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