Subject:	**HOUSING REVENUE ACCOUNT BALANCES**
Meeting and Date:	**Special Cabinet – 24 September 2013** **Scrutiny (Policy & Performance) Committee – 24 September 2013** **Special Cabinet – 25 September 2013** **Extraordinary Council – 25 September 2013** **Governance – 26 September 2013 (Members are requested to bring this report to the Governance meeting, as the attachments to this report may be referred to in the discussion on the 2012/13 outturn report and statement of accounts).**
Report of:	**Mike Davis, Director of Finance, Housing and Community**
Portfolio Holder:	**Councillor Sue Chandler, Portfolio Holder for Housing, Children's Services and Safeguarding, Youth and Community Safety and Councillor Mike Conolly, Portfolio Holder for Corporate Resources and Performance**
Decision Type:	**Non-Key**
Classification:	**Unrestricted**
Purpose of the report:	To approve the transfer of £12.5m of credit balances in the Council's 2012/13 accounts from the Housing Revenue Account (HRA) to the General Fund (GF).
Recommendation:	That Cabinet recommend that Council approve the transfer of £12.5m of credit balances from the HRA to the GF, in the Council's 2012/13 accounts, in accordance with Schedule 4, Part III, paragraph 2 of the Local Government and Housing Act. That Council approve the transfer of £12.5m of credit balances from the HRA to the GF, in the Council's 2012/13 accounts, in accordance with Schedule 4, Part III, paragraph 2 of the Local Government and Housing Act.

1. **Summary**

1.1 The introduction of HRA self-financing in 2012/13 was accompanied by the abolition of housing subsidy in the HRA. Schedule 4, Part III, paragraph 2 of the 1989 Local Government and Housing Act has always provided as follows:

1.2 *"A local housing authority to whom no Housing Revenue Account subsidy is payable for any year may carry the whole or part of any credit balance shown in their Housing Revenue Account for that year to the credit of some other revenue account of theirs".*

1.3 The advice of the Council's Treasury Management advisers, Capita (formerly known to Members as Sector), and the Solicitor to the Council, is that it would be permissible to make a transfer from the HRA to the GF, in the 2012/13 accounts of some, or all, of the accumulated credit balance in the HRA as at 31st March 2013 (see Appendix 1).

1.4 The ability for English housing authorities to make this transfer will cease as from 1st October 2013, following the coming into force of the Localism Act 2011 (Commencement No. 9) Order 2013.

1.5 Therefore the Council has a short period, ending on 30th September 2013, during which it can decide whether to make a transfer from the HRA to the GF.

1.6 In view of the potential implications and opportunities created by such a transfer, and the fact that it would be outside of the current budget and policy framework, this is a matter for Council to consider and decide.

1.7 As at 31st March the HRA (as shown in the accounts to be presented to Governance for approval on 26th September) had a balance of £13.1m.

1.8 In considering this matter, Members will need to decide:

(a) Should the Council make any transfer of the HRA balances to the General Fund? And

(b) If so, how much should be transferred?

2. Introduction and Background

2.1 The HRA is currently a ring-fenced account.

2.2 The bulk of the properties within the HRA were constructed from public funds before the HRA was "ringfenced" by the Local Government and Housing Act 1989. Before ringfencing, the HRA and GF were not separated in the same way, and the HRA would frequently receive financial support from the GF. In addition, a significant proportion of the balances have accrued from rental income supported by Housing Benefit funded from general taxation.

2.3 After ring-fencing many HRA's ran at a deficit, and received support by way of housing subsidy from central government. This was funded, in part, by "negative subsidy" paid by the HRA's that were in surplus. Overall, the system was balanced or supported by central government funds. The advice from Capita at Appendix 1 provides more detailed background on these issues.

2.4 However, in recent years, a large proportion of the HRA's, including Dover's, moved to a position of "negative subsidy", where they made payments to government and the system, at a national level, was in surplus – with government using the surplus for other purposes.

2.5 This arrangement came to a close with the introduction of "self financing" from 2012/13. Authorities paying a negative subsidy to government were required, by government, to pay a significant sum to government as a means of buying themselves out of the annual negative subsidy payments.

2.6 In Dover's case, for 2011/12, the last year of the subsidy system, DDC paid £5.9m to government, and this figure was increasing annually. In contrast, after borrowing £90.4m from the PWLB and paying it to government, the HRA now has to pay £4.7m per annum to the PWLB to service the new debt. The HRA is circa £1.2m per annum better off under the new system.

3. **Sustainability of the HRA**

3.1 Any consideration as to the amount (if any) that should be transferred from the HRA to the GF needs to take into account the HRA's current and future position.

3.2 The 2012/13 unapproved accounts[1] circulated to Governance currently show an HRA balance of £13.1m[2]. In addition the HRA budget for 2013/14 forecasts a further £1.7m surplus and the HRA business plan forecasts generally increasing surpluses for the coming years.

3.3 In order to project the impact of transferring balances to the general fund, modelling has been undertaken, to demonstrate the impacts of transferring £12.5m to the general fund (see Appendix 2). To test for sensitivity this has also been modelled with transfers of £11.5m and £13.0m.

3.4 These show that, other than the level of balances held, and a very small difference in the interest receivable, all three options are sustainable in the short, medium and long term.

3.5 In this modelling the following factors have been taken into account with regard to the HRA revenue budget:

(a) Rent Increase

The assumed rent increases are CPI+1% in accordance with recent government proposals.

(b) General Inflation

This has been assumed at 2.5%.

(c) Rent collection rates and bad debt provision

Rent collection has been assumed to be maintained at broadly the current levels, but with an assumed increase in bad debt provision to allow for the possible effects of welfare reform. The plan therefore provides for bad debts of £250k per annum. In 2012/13 bad debt provision was £64k.

(d) Interest on cash balances

An initial loss of interest on cash balances has been assumed, following the transfer. This has then been re-introduced to reflect the re-establishment of HRA balances through future surpluses.

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[1] To be presented to Governance for approval on 26th September 2013.

[2] This currently comprises £5m in the earmarked Housing Initiatives Reserve and £8.1m in general balances. There is also £250k in the Tenants Compact Reserve, but this has not been included in the current proposals, and will remain at the tenants' disposal.

(e) Debt repayments

The debt repayments (of combined capital and interest) on the borrowing required for self-financing are fixed in cash terms over the 30 year term, and therefore as rental income increases, the HRA's financial position is expected to improve.

(f) Basis of assumptions and projections

The data in Appendix 2 are forecasts and projections, not budgets. Accordingly, they cannot be developed with precision, therefore a prudent and conservative approach has been taken, with expenditure assumed to be at the higher end of expected ranges, and income at the lower end.

(g) Impairment

Members should be aware that, from 01/04/2012, regulations were introduced requiring local authorities to charge impairment losses on revaluation of HRA assets against revenue balances where they cannot be absorbed by past upward revaluations. The regulations exclude HRA dwellings for a period of five years and for the interim period affect HRA non-dwelling assets such as garages and shops only.

From 01/04/2017 impairment losses on dwellings will be included and with a property portfolio of circa 4,400 properties, a loss of value averaging just £1,000 per property, would lead to an impairment charge of £4.4m.

Where this can be absorbed by the revaluation reserve, if it has previously benefited from increases in value, the issue is not a problem. Where this is not the case, then the impact would be charged to the HRA balances.

House prices are currently at a comparatively low point in their cycle (certainly within the Dover district). It follows that any short term price movement is expected to be upwards. If this happens the increased valuations will be posted to a "revaluation reserve", where they will remain. If there are subsequent reductions in values, they will simply erode the revaluation reserve balance.

Therefore, any impairment will only start to impact on the HRA if values fall below their current level, as carried on the Council's balance sheet. This, together with the robust position of the HRA and the rate at which reserves will be rebuilt, all place DDC's HRA in a stronger position to deal with impairment than many HRAs.

Members should also note that this is purely an accounting entry and if it is seen to be creating unsustainable problems to HRAs generally, it is difficult to envisage a situation where the requirement will not be removed by the DCLG.

(h) Overall variation in the baseline for 2013/14

The current 2013/14 surplus is forecast to be £1.72m. The (prudent) re-working of the 2013/14 budget shows a forecast of £1.143m.

The variation of £577k reflects the impacts of the transfer (primarily reduced interest on cash balances) and other variations as follows:

Variance Analysis	£k
Term maintenance – increased expenditure advised by EKH	50.0
Increased voids advised by EKH	100.0
Loss of interest	138.0
Increased EKH management fee	65.0
ICT Investment	28.0
Sheridan Road Play Area	48.0
Structural repairs	100.0
Other	48.0
Total	**577.0**

3.6 The following factors have been taken into account with regard to the HRA's capital and major projects.

(a) Whitfield

£2.5m was specifically allocated for development at Whitfield, and was to be used to build / commission 26 units of social housing to be retained within the HRA.

However, following further discussions with the developer, the Council has indicated that it intends to exercise its option to acquire the land at Whitfield and seek a development partner (probably an RSL) to build the 26 affordable units on the land, and to support this through a GF grant as gap funding, using a proportion of the reserves transferred from the HRA.

(b) Sheltered Housing Scheme

Funding of £1.8m has been allowed for the planned refurbishment and remodelling of one of the Council's sheltered housing schemes, and this investment accounts for the dip in the level of surplus in 2014/15.

(c) Single Housing ICT System

East Kent Housing are assessing the business case for the procurement of a single housing system for the EKH partnership. £350k has been included as the Council's estimated potential share of this project.

(d) Structural Repairs

An additional £100k per annum has been provided, including provision for reconstruction of retaining walls that are nearing the end of their life.

(e) Investment in the existing stock

The Council's current housing stock meets the decent homes standard and the current plan enables us to exceed this standard.

In addition, the council has signed up to the "green deal" providing tenants with access to loft and cavity wall insulation to address inefficiencies in the existing properties and mitigate fuel poverty.

The HRA business plan indicates that future balances will be generated, from which additional investments could be made.

(f) HRA Capital Headroom

As the HRA pays off circa £1.8m per annum of its outstanding debt in the early years, it is creating headroom for additional borrowing, should that be required. By the end of 2013/14, this headroom will be circa £3.6m, rising to £20m by 2022. If there is an urgent call for HRA capital resources, this could be provided by additional borrowing.

3.7 Overall, the revenue budget is robust and closely monitored. The capital programme is fully funded and also closely monitored, and therefore the HRA could sustain a transfer of £12.5m without undue risks.

4. **Benefits to the Council**

4.1 The primary benefits to the Council are flexibility and sustainability.

4.2 If the balances were to remain within the HRA then, after 30 September, they could only be used for the specific purposes of the HRA. By transferring the balances to the general fund, they can be applied to the whole range of General Fund purposes. These could include, but are clearly not limited to:

(a) The provision of additional housing, outside of the HRA, through direct construction / purchase or by financial assistance to Registered Social Landlords (RSLs);

(b) The potential to increase Disabled Facilities Grants;

(c) The maintenance of statutory services which could otherwise, in 3 – 4 years time, become unsustainable;

(d) The development of a financial strategy to sit above the Medium Term Financial Plan (MTFP), and to consider significant scale investment projects that would assist the council in working towards a sustainable model that could cope with total loss of the Revenue Support Grant (RSG) within 5 – 10 years.

5. **Financial Strategy**

5.1 In considering the development of a financial strategy, the Council will analyse its projected resource base and whether it should plan its baseline budget to be as self financing as possible, so as to prepare for potential further losses in RSG.

5.2 The Council also needs to take into account the additional uncertainty and volatility in its resourcing and expenditure as a result of reducing RSG, the Council Tax

Reduction Scheme, the Localisation of Business Rates, the top slicing of New Homes Bonus and the range of welfare reform initiatives.

5.3 In the light of these uncertainties, a higher level of balances, if achievable, would be prudent.

5.4 The 2013/14 budget shows:

Financing	2013/14 Budget £000	%
Revenue Support Grant (RSG)	3,481	23.7
NDR (Business Rates)	3,237	21.9
Council Tax Support Funding	1,218	8.3
Council Tax	5,822	39.5
New Homes Bonus	927	6.3
Collection Fund Surplus	37	0.3
Sub Total	**14,722**	**100.0**
Impact of Business Rates Redistribution	-243	
Total	**14,479**	

5.5 If the government do withdraw all RSG over the coming 5 – 10 years, then that would equate to a reduction of circa 23.7% in overall resourcing. From 2014/15, the Council Tax Support Funding will be rolled into the RSG, so if that is also withdrawn the reduction could be as high as 32%.

5.6 In addition, although the New Homes Bonus was originally presented as a secure, stable income stream, government now propose to top slice, and re-distribute via the LEP. Therefore the NHB available to DDC is likely to reduce and there is no certainty that NHB top sliced from DDC and paid into the LEP is spent in Kent, let alone East Kent or Dover.

6. Impacts upon the services provided to tenants

6.1 The HRA's baseline budget is robust and is operating at a surplus which, with rent convergence and capped debt charges to the PWLB, is forecast to be maintained and to grow.

6.2 Therefore, no detrimental service impacts to HRA tenants or additional rent increases will arise as a direct result of this proposal. This is supported by the advice from Capita – see paragraph 2.9 of Appendix 1.

7. What would happen to the balances after transfer to the General Fund

7.1 After transfer, the balances would still remain under the Council's control. Transfer does not imply authority to spend. The balances would remain under the same controls and budgetary processes as existing resources.

7.2 The 2014/15 budget and the Medium Term Plan 2014/15 – 2017/18 are being prepared. If the transfer is approved then they will be reflected in the budget and MTFP, together with a strategy for their use and detailed of any proposed specific applications. This will be subject to Cabinet and Council decisions and Scrutiny.

8. **Views of the Councils Auditors and Advisers**

8.1 Grant Thornton (GT), the Council's auditors, have been advised of the proposed transfer and are not minded to challenge it.

8.2 The auditors also confirm that the opportunity to make this transfer ends on 01/10/13 and advises that we have to satisfy ourselves that in exercising the discretion to make any transfer we can reasonably demonstrate that we have done so lawfully. In particular we need to adequately consider:

(a) The power to do so;

(b) The impact on the HRA and the HRA Business Plan;

(c) The risks;

(d) The year of account in which the entry should be made and whether the transfer is for the accumulated credit at the time of transfer, or the surplus for that year;

(e) Governance issues.

8.3 The Council's advisers, Capita, have also been consulted. Their advice and views are contained in Appendix 1. This report is consistent with their views.

9. **Terms and Conditions**

9.1 It is important that, in considering the transfer, Members understand that they cannot, at present, reverse the transfer, and this position is unlikely to change. They should also understand the limitations and flexibilities that will follow the transfer. In particular, once transferred, the funds cannot generally be used:

(a) To support continuing HRA activities;

(b) To support capital expenditure for HRA (although there may be some scope for flexibility around this point);

(c) For the purchase or construction of housing to be run by the council as part of any social housing scheme.

9.2 The funds can be used to:

(a) Provide grants to RSLs;

(b) Fund the construction of housing for sale or for commercial operation (ie not social housing);

(c) Fund any other general fund revenue purpose;

(d) Fund any other General Fund capital purpose.

10. **Risks**

10.1 Unexpected HRA deficit.

10.2 The HRA budgets and business plans have been robustly produced, and have proved reliable. Therefore this risk has been mitigated and the residual risk is regarded as low.

10.3 Urgent capital requirement

10.4 The HRA is forecast to remain in surplus, thus rebuilding its reserves, which will be available for capital purposes if required. However, the capital headroom for borrowing is increasing as the existing debt is repaid, creating capacity for additional capital funding if required.

10.5 Welfare reform

10.6 The impact, so far, of welfare reform, has been relatively modest. However, the future projections have included modelling the impact of a reduction in rent collection rates and an increase in bad debt provision. Nonetheless, the HRA is projected to remain in surplus.

10.7 Loss of budgetary control.

10.8 DDC staff have retained control over the HRA, and undertake continuous budget monitoring through the year, based on information from EKH, to ensure that any adverse and unsustainable trends are identified early and corrective action taken. The mitigated risk is considered low.

11. **Identification and Evaluation of Options**

11.1 First decision:

(a) Make a transfer

(b) Do not make a transfer

11.2 If the transfer is not made, the GF's ability to cope with its reducing resource base, and in particular, its ability to invest in transformational change, is severely limited. For this reason this is not the recommended option.

11.3 If the transfer is made, then the General Fund will have the flexibility and resources to invest in changes that will better enable the Council to operate within the more constrained resourcing level it faces. For this reason, this is the recommended option.

11.4 Second decision:

(a) £12.5m

(b) £11.5m

(c) £13.0m

11.5 Transferring £13.0m of balances would leave the HRA with minimal balances during 2013/14 to cope with any unexpected (albeit unlikely) additional pressures.

11.6 Transferring £11.5m does not maximise the opportunity available.

11.7 Transferring £12.5m provides the HRA with a reasonable cushion, but still maximises the opportunities available to the GF. For these reasons this is the recommended option.

12. Changes to the Accounts

12.1 Appendix 3 contains changes to the accounts that would be made if the £12.5m transfer is approved. The changes would be identical, save for the specific amount, if some other transfer were approved.

12.2 It is proposed that Governance will approve the final accounts based on incorporation of Appendix 3 into the accounts.

13. Equalities Impact Assessment

13.1 The proposed transfer is an accounting entry that does not have a direct or immediate impact on the services provided by the council, nor does it provide authority to spend on any particular service.

13.2 The resources transferred could continue to be used to support the provision of social housing via an RSL, or for any other General Fund purpose.

13.3 The transfer does not prevent the Council from pursuing its objectives in compliance with the public sector equalities duty.

14. Corporate Implications

14.1 Comment from the Section 151 Officer: Finance have produced this report, and therefore have no comment to add.

14.2 Comment from the Solicitor to the Council: The Solicitor to the Council has been consulted in the preparation of this report and has no further comments to make.

14.3 Comment from the Equalities Officer: The Equality officer has been consulted during the development of this report and has no further comments to make other than to remind members that in discharging their responsibilities they are required to comply with the public sector equality duty as set out in section 149 if the Equality Act 2010 http://www.legislation.gov.uk/ukpga/2010/15

15. Appendices

Appendix 1 – Advice from Capita

Appendix 2 – Modelling of HRA Business Plan and Transfer Values

a) £12.5m

b) £11.5m

c) £13.0m

Appendix 3 – the changes to the 2012/13 accounts if the proposals are approved (assuming a transfer of £12.5m).

16. **Background Papers**

(a) Medium Term Financial Plan 2013/14

(b) HRA Business Plan

(c) 2012/13 Accounts

(d) Local Government Act 1988

(e) The General Consents under section 25 of the Local Government Act 1988 (Local Authority assistance for privately let housing) 2010

(f) 1989 Local Government and Housing Act

(g) Localism Act 2011 (Commencement No. 9) Order 2013.

Contact Officer: Mike Davis, Director of Finance, Housing and Community

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