APPENDIX 1

CAPITA

Asset Services

# Consideration of Issues in Connection with the Potential Transfer of HRA Credit Balances

## Contents

## 1. Introduction

1.1 Capita Asset Services (Treasury solutions) has advised the Authority that there is a provision within the legislation that governs Housing Revenue Account (HRA) accounting requirements which provides housing authorities with an ability to transfer any credit balance on the HRA to any other revenue account, which will in essence be the Authority's General Fund (GF).

1.2 Under normal circumstances the HRA is a "ring fenced" account, whereby there are strict rules governing the manner in which expenditure and income for HRA services must be accounted for. In essence, these restrict an authority from charging, crediting or otherwise transferring money between their HRA and General Fund.

1.3 Following the introduction of HRA Self Financing, local authorities have ceased to qualify for the receipt of housing subsidy in the manner which applied until 31st March 2012. Consequently, a little appreciated provision within the governing legislation became operational, which allows the Authority to transfer any credit balance on their HRA to their GF.

1.4 This provision only has effect until 30th September 2013, after which time the provision is repealed.

## 2. Past Inequities between the General Fund and the HRA

2.1 Although the accounting requirements which have since 1989 governed HRA accounting have had the intention of ring fencing the costs and benefits which are considered to only have relevance to the social housing function, the accounting treatment of certain matters is known to cause, or have caused, significant financial disadvantage to authorities' General Funds both over many earlier years, and for the future.

2.2 The most recent factor concerns the treatment of capital receipts. All capital receipts have always been the property of GF, regardless of the asset from which they derive. This situation remains, as all assets are owned by the authority. However, a recent statutory change means that capital receipts arising from the sale of an asset previously held for housing purposes must in future be used for an HRA purpose if the authority wishes to avoid the prospect of having to increase their GF loan interest costs. There is no financial justification for such a change/cost increase for GF, as the cost of the assets which gave rise to the capital receipt has always been met from subsidy. HRA tenants have never borne any of the costs, but will in future receive benefits that were not envisaged as part of the HRA self financing settlement.

2.3 The extent to which GF was able to recharge the HRA in respect of that account's relevant proportion of loan interest has been inappropriately assessed over a number of years. The recharge arrangements were complex, but in essence the HRA did not bear its proper share of loan interest costs because of the manner in which the consolidated rate of interest was calculated. This anomaly has been recognised since the introduction of self financing, but there is no ability for earlier discrepancies to be adjusted for through the ongoing interest recharge process.

2.4 Further costs to the GF arose from the consequences of the statutory Right to Buy facility (RTB). Local authorities had borrowed long term over many years for an HRA debt liability which they assumed would always be covered by housing subsidy. However, the introduction and ongoing effect of RTB resulted in a reduction of the amount of housing debt liability which qualified for recharge/subsidy, and caused GF to be left with having to bear a greater share of higher interest loans under the recharge process in a market situation which was resulting in rapid reductions in interest rates.

2.5 The above mentioned reduction in HRA debt liability also caused additional premium (i.e. rolled up interest) costs to be borne by GF. Premium costs arise when loans are rescheduled with a view to achieving a reduction in annual revenue costs. Higher interest rate loans taken out to finance an increase in HRA capital debt liability were invariably only capable of being rescheduled a few years after the associated debt was offset by RTB amounts "set aside". Instead of the premium liability being borne by the HRA in relation to its debt liability

at the time the loans were taken out, it was calculated in relation to the reduced amount following set aside during an intervening period.

2.6 In order to achieve a revenue interest cost reduction through rescheduling, the premium cost was capable of being spread over the period of replacement loans. However, until the premium was charged to revenue, there was an interest cost of financing it. The housing subsidy rules did not allow for the HRA share of these costs to qualify for subsidy, which almost always resulted in the whole of the premium financing cost being borne by GF, including the HRA element.

2.7 There were also many problems with the manner in which the 3 month LIBID factor was assessed within the CFR/earlier CC debt liability which become more complex to explain, but which in essence had the effect of increasing the GF share of loan interest in an inequitable manner.

2.8 In terms of the current level of HRA balances, these may or may not appear to be at a level which indicates a surplus over monies required for other HRA purposes. However, the nature of self-financing, and the manner in which future expenditures and income within the HRA have been assessed, is likely to result in considerable increases in HRA balances in future years. If, therefore, it is wished to recompense GF for past inequalities, it may be necessary to consider deferral of non priority HRA expenditures if this is a requisite to take advantage of this one off opportunity.

2.9 Perhaps the key point to make is that the transfer of balances in this manner should not in any way cause tenant costs through rents to increase. Rent levels are controlled by statute, and are subject to pre-determined levels of increase.

## 3. Statutory Provisions

3.1 The HRA accounting requirements are governed by the Local Government and Housing Act 1989, along with certain Determinations made under these legislative provisions.

3.2 Under Schedule 4 of the Act, a local housing authority to whom no housing subsidy is payable for any year may carry the whole or part of any credit balance shown in their HRA for that year to the credit of some other revenue account of theirs.

3.3 It appears likely that this provision was made in recognition of the fact that once an authority ceased to have the ability to influence the manner in which housing subsidy was distributed or redistributed, it could choose to benefit from any monies considered to be surplus to HRA requirements in cases where this was considered appropriate.

3.4 In recognition of the fact that housing subsidy arrangements have now ceased, a clause within the Localism Act 2011 has determined that the provision which allows for balances to be transferred in the manner explained above shall be repealed, effective from 1st October 2013.

3.5 Because the HRA represents essentially a landlord account for revenue transactions, it is only the particular provision of Schedule 4 which has enabled a transfer of balances to take place. Outside of this, the ring fence rules determine that it is not possible for a transfer of balances to be made back to the HRA, either now, or at any future date.

3.6 In terms of commenting upon the fact that the statutory wording relates to a transfer of balances "shown in their HRA for that year", under certain circumstances, an authority might assess the amount of its HRA credit balances at a year end, and decide at that time to transfer an amount of credit balances. Under such circumstances, the credit balances would not be credited to the HRA for the following year, in accordance with Schedule 4, Part I, Item 10. However, if this ability to transfer is not capable of being included within the accounts for 2012/13, the total amount of credit balances available at 31st March 2013 would be credited to the HRA on 1st April 2013. This would then represent an amount of HRA credit balance in respect of the whole of the 2013/14 financial year.

3.7 Although it is common practice for an authority to make certain determinations with regard to its balances when their amount is

ascertained at the end of a financial year, this cannot detract from the authority's ability to consider and make such a transfer at any time. Legislation does not specify that this must be an end of year transaction, and it would be difficult to imagine that there should ever be such legislative intent, as it would not serve any particular purpose or objective.

3.8 We have however suggested that it would be necessary for an authority to demonstrate clearly that it has carried out any such transfer in accordance with a properly authorised decision of the authority, and for the appropriate accounting entry to be made recording the transaction before the 30th September 2013.

## 4. Other Matters

4.1 In terms of the appropriateness of the amount to be transferred. In general this is a matter for each authority, although the decision should clearly take careful account of the likelihood of the HRA remaining in balance for the foreseeable future. Much will depend upon whether present rent levels, and statutorily permitted levels of rent increase, along with other income, are likely to more than offset expenditure for each financial year.

4.2 It may be that the forecast amounts of net expenditure for each year are adequately supported by the authority's budget and business plan.

4.3 In the same manner as the ring fence applies to the transfer of GF revenue monies from the GF to the HRA, it is not possible for the authority to use GF credit balances to finance new capital expenditure that is for an HRA purpose.

4.4 Schedule 4 provides that amounts of capital expenditure may be debited to the HRA in respect of houses or other property within the account, but this expenditure may only be offset by statutorily authorised credits to the HRA. Essentially, this provision is referring to those items of HRA capital expenditure which an authority decides shall be financed directly from HRA revenue resources.

4.5 Other amounts of capital expenditure will be incurred by an authority as a whole. The Item 8 Determination provides that loan interest charges to the HRA shall be made in accordance with proper practice, after having regard to the amount of the HRA Capital Financing Requirement (CFR). The HRA CFR represents the HRA proportion of an authority's aggregate debt liability (i.e. aggregate CFR). New capital expenditure which is not financed from available resources has the

effect of increasing the CFR and, in the case of capital expenditure in respect of houses and land accounted for within the HRA, the HRA CFR.

4.6 Although there is no direct means by which the Authority may pass revenue monies back to the HRA following a transfer of balances, there are a number of ways in which recharges may be properly rearranged so that the effect is the same.

4.7 We shall be happy to advise the Authority in greater detail in this respect should they so wish. But in general, there is scope within accepted practices for the manner in which loan charges are recharged to the HRA to be subject to a number of discretions. For example, in cases where amounts of HRA debt liability are effectively financed by the Authority itself under its overall treasury management policy, it is possible for a range of different interest rates to be used for the purpose of recharging the HRA.

4.8 Similarly with a range of other recharges. Costs associated with housing welfare services, grounds maintenance, shops, open spaces, community centres and playgrounds are examples of those which may be considered with regard to the wider benefits they may bestow. This is by no means a rigid accounting or statutory compliance area, and is capable of offering acceptable alternative accounting arrangements should an authority wish to pursue such opportunities in greater depth.

4.9 In terms of using monies transferred for new building purposes. It is not in our view possible for the Authority to use GF monies for the purpose of providing social housing. Although local authorities have been given a General Power of Competence under the Localism Act 2011, this power is constrained by any pre existing limitation.

4.10 Because there are clear powers within Part II of the Housing Act for the provision of social housing, and the manner in which this should be accounted for, we consider that any attempt to override this requirement, with the associated implications of avoiding RTB and HRA accounting and debt cap implications, could be construed as an abuse of power, and held to be *ultra vires*.

4.11 These comments would not, however, apply to the provision of market or other forms of commercial housing. We consider that such expenditures could be carried out in reliance upon the General Power of Competence. There is, however, a prospect that such action could only be carried out through the formation of a controlled company.

4.12 Similarly, the Authority would have the power to grant financial assistance to an RSL in accordance with, and subject to the limitations of, the power provided by S.24 of the Local Government Act 1988.

4.13 This report has, for expediency, been prepared in a manner which highlights the key matters that the Authority may wish to consider, without setting out in greater depth the underlying more detailed considerations which we consider would apply to matters such as providing financial assistance to an RSL, or transferring land at less than market value. These are matters that we would be happy to explain in greater depth should the Authority so require.