Supplementary Committee Agenda

Epping Forest District Council

Finance and Performance Management Cabinet Committee
Tuesday, 18th May, 2010

Place:	Committee Room 1, Civic Offices, High Street, Epping
Time:	6.30 pm
Democratic Services:	Gary Woodhall (The Office of the Chief Executive) Tel: 01992 564470 Email: gwoodhall@eppingforestdc.gov.uk

---

6. REPLACEMENT OF HOUSING REVENUE ACCOUNT SUBSIDY SYSTEM (Pages 3 - 20)

(Director of Finance & ICT) To consider the attached report (FCC-025-2009/10).

This page is intentionally left blank

Report to the Finance and Performance Management Cabinet Committee

Epping Forest District Council

Report Reference: FCC-025-2009/10
Date of meeting: 18 May 2010

Portfolio: **Housing**

Subject: **Response to CLG offer on the reform of the HRA subsidy system**

Responsible Officer: **Brian Moldon** **(01992 564455).**

Democratic Services: **Gary Woodhall** **(01992 564470).**

Recommendations/Decisions Required:

(1) To note the attached report provided by Consult CIH Ltd;

(2) To recommend to the Cabinet the rejection of the proposed offer from CLG on the reform of the housing subsidy system and to approve the draft response at appendix 2 (to follow) to the CLG consultation; and

(3) To note that a further report will be provided on the possible transfer to the General Fund of non-housing assets currently held within the Housing Revenue Account (HRA).

Executive Summary:

A prospectus was issued on 25 March 2010 detailing how the Government wishes to dismantle the current HRA subsidy system, replacing it with self-financing through a debt re-allocation settlement. The offer gives an opportunity for the Council to have full control and responsibility in running the HRA and initial workings indicate that it would benefit the HRA. However, the proposed offer does have an adverse effect on the General Fund which would require the Council to find over £2m to cover the interest and Minimum Revenue Provision (MRP).

Reasons for Proposed Decisions:

To be able to respond to the CLG consultation on the proposed dismantling of the HRA subsidy system.

Other Options for Action:

To respond in favour of the offer and / or to make changes to the draft responses in appendix 2 (to follow).

Report:

<u>Introduction</u>

1. In July 2009, the Department for Communities and Local Government (CLG) published a Consultation Paper "Reform of Council Housing Finance" following a review of council housing finance which began in March 2008. The problems with the current HRA subsidy system, addressed in the review, are many and varied. They include:

- Lack of transparency and accountability between landlords and tenants;
- Growing complexity in the way resources are distributed;
- Increasing volatility in funding allocations making planning very difficult; and
- Since 2007, the system being in overall surplus – so that an element of tenants rents supports other Government spending, not just (as was previously the case) spending by other housing authorities.

2. Following the conclusion of the consultation on HRA reform at the end of October 2009, CLG has been working on a prospectus (which came out on 25 March 2010) for a voluntary offer to local authorities to buy themselves out of the current HRA subsidy system.

3. At Cabinet on 1 February it was agreed that once the offer had been made by CLG that this Committee be requested to consider the issues and to recommend to the Cabinet a response from the Council. It was also noted that the appointment of Consult CIH Ltd would be made to advise the Council on all the issues relating to the offer.

<u>Impact on the HRA</u>

4. We have now received the report from Consult CIH Ltd this is attached at Appendix 1 for your information. The report primarily considers the consequences for the HRA and more briefly touches on the impact on the General Fund. The key findings from this report are:

(a) The debt allocation to this Council is £180m, for buying ourselves out of the current HRA subsidy system. However, the Government would expect the Council, through the General Fund, to pay back the HRA the money it has borrowed from it, so that it can off set some of this debt. This loan equates to £22m and would reduce the debt down to £158m.

(b) Management and Maintenance Allowance increase by 3.1% and Major Repairs Allowance by 25.6%, This is slightly below the national average uplift.

(c) The Council will be able to keep **all** of it's rents received, currently we pay over to CLG £10m in subsidy (for 2010/11), which is the difference between what we collect in and what CLG believes we need to spend on our housing stock.

(d) The annual cost to the HRA of servicing this new debt will be £9.5m (based on £158m).

(e) A revised HRA business plan has been created and its shows that the HRA remains viable, with the ability to meet the asset management expenditure requirement each year. Furthermore, it shows that our debt will be repaid in 18 years. The sensitivity analysis provided shows the maximum period of time it would take to repay the debt is 21 years if some of the variables prove worse than the base model.

(f) The offer also gives the opportunity for the HRA to build new homes.

(g) In the future all Right to Buy receipts will be kept by the Council, currently 75% (less administration costs) of our Right to Buy receipts are paid to CLG. However, there will still be a restriction of 25% that can be used for the General Fund, as before, the remaining 75% has to provide for "affordable housing".

5. The report suggests that the HRA would be better off under this voluntary offer, as the Council would have full control and be able to keep the full rents to spend on ensuring the housing stock are kept to a decent standard, with capacity to repay the entire debt within 18 years.

6. The prospectus however makes reference to a "full and final settlement" and it is evident that the subsidy system would be virtually impossible to put back together again if it is

dismantled. Nevertheless, there are references to circumstances in which the settlement might be revisited and this is a cause for concern.

7. The debt per property for this Council will be around £27,500, this is at the top end of the debt per property for Council's across the Country. It appears CLG assume we have a high surplus of cash, compared to some other authorities, where rents are lower and they have yet to achieve Decent Homes for their housing stock. So although the HRA will be better off under this proposal, we could have been much better off, if we had received a smaller debt per property.

8. A consequence of this high debt per property, is that our HRA will have less ability to take on other further debt if the Council wants to build new homes. This is relative to some authorities, who benefit from lower debt but do not face such high levels of demand for new housing. This could be viewed as this Council being penalised for having managed its housing stock and finances well in the past.

9. The proposal appears good when compared to the current subsidy system. However, there is a fundamental question of whether it is fair for this Council to have to take on £180 million of debt that has been created by the spending of other authorities.

Impact on the General Fund

10. Traditionally, local authorities have held all of their debt in one single 'pool' across all services within the General Fund. With the introduction of self financing for the HRA, the government is seeking to encourage authorities to separate the debt and therefore increase transparency around the costs of debt charges to tenants.

11. This Council is debt free and has a negative overall requirement to borrow, known as the Capital Financing Requirement, as the amount by which the HRA is negative (i.e. in surplus) outweighs the positive (debt) General Fund CFR as shown below:

- General Fund £22.019m
- HRA -£22.803m
- Overall -£0.784m

12. Should the Council take on this new debt, then the HRA CFR would change to £157.644m, the Council's standing would no longer be considered debt free with an overall positive CFR of £179.663m. Authorities' that are not overall debt free are required to make debt repayments, known as Minimum Revenue Provisions (MRP).

13. Currently our General Fund pays interest at 1.8% (the average rate of return on our investments for 2009/10) to the HRA on £22m, an annual charge of £396,000 (for 2008/09 this was 5.5% which totals £1.2m). If the proposed debt re-allocation takes place this internal borrowing will be replaced with an external loan, likely to be in the region of 6%, and a Minimum Revenue Provision of £880,000 (4%). This would produce a new combined charge to the General Fund of £2.2m, an increase of £1.8m on the current position (increase of £1m against the 2008/09 accounts).

Impact of the proposed system

14. The prospectus indicates that there would be a benefit to the HRA with the proposed new debt being repaid within 18 years and the Council able to meet the asset management expenditure requirement each year. However, the Council's General Fund would have a significant additional cost imposed on it by the current proposal.

Non Housing Assets within the HRA

15. Non Housing Assets within the HRA relates to the commercial properties, this includes

shops in the Broadway and elsewhere, petrol stations and pubs. The proposed model discussed above does not include any of the rental income from these commercial properties and it still shows the HRA is viable without including these rents.

16. In carrying out this exercise it has been highlighted that there is a possibility that these assets can be transferred to the General Fund thereby, the rental income would become income to the General Fund rather than the HRA. The market value of the asset being transferred would need to be added to the General Fund CFR increasing its positivity and taken from the HRA CFR increasing its negativity. The net result would be an increase in interest payable by the General Fund to the HRA.

17. A benefit to the General Fund would occur as long as the rent received, net of property expenses, exceeded the additional interest payable to the HRA. Further work will be undertaken on this exercise to establish the impact on both the General Fund and HRA, and a report will come back to Cabinet in the coming months.

Resource Implications:

Under the offer, the Council would no longer make subsidy payments in the region of £10m per annum. However, the HRA would need to make an interest payment on the new debt in the region of £9.5m. The General Fund would suffer significantly and incur additional costs of approximately £1.8m.

Legal and Governance Implications:

The Housing and Regeneration Act 2008 (S313) gives Councils the opportunity to voluntarily come out of the housing subsidy system. If a large number of Councils decide not to come away from the current system, the offer will probably be withdrawn and the government may then legislate. It is possible that any incoming government may not see this as a legislative priority or may revisit the sharing out of the debt to give greater headroom to Councils in areas of highest demand for new social housing.

Safer, Cleaner, Greener Implications:

None.

Consultation Undertaken:

Consult CIH Ltd has been appointed to advise the Council on all the issues relating to the proposed offer. The Tenants and Leaseholders Federation has also been invited to provide their views on the proposed offer. There are 170 local authorities within the subsidy system, however, there are only 9 authorities with negative CFR like EFDC. A letter has been sent to these 9 authorities drawing their attention to the affect on the General Fund and seeking their views and whether they would be willing to do a joint response through the Local Government Association or direct to the CLG.

Background Papers:

Cabinet 1 February 2010 “Response to an expected CLG offer on a proposed debt re-allocation or settlement to replace the Housing Revenue Account (HRA) subsidy system”.

Impact Assessments:

<u>Risk Management</u>
The offer, although in “full and final settlement”, includes a reference that the debt could be revisited and the allocation changed. The repayment profile within the model assumes that the debt is like a capital and interest mortgage, in reality the debt would be arranged in chunks and therefore to repay earlier would incur redemption penalties, or if we would need

to refinance during the course of the 30 year plan, interest rates may be different to those in the model.

Equality and Diversity:

Did the initial assessment of the proposals contained in this report for relevance to the Council's general equality duties, reveal any potentially adverse equality implications?	No
Where equality implications were identified through the initial assessment process, has a formal Equality Impact Assessment been undertaken?	N/A

What equality implications were identified through the Equality Impact Assessment process?
N/A

How have the equality implications identified through the Equality Impact Assessment been addressed in this report in order to avoid discrimination against any particular group?
N/A

This page is intentionally left blank

Epping Forest District Council
Council Housing: a real future
Report 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 Epping Forest District Council. This note sets out the main findings of the modelling work, highlights the main Epping Forest-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 Members and Tenants and Leaseholders Federation 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

ConsultCIH Ltd
4 Riley Court,
Millburn Hill Road,
Coventry, CV4 7HP

www.consultcih.co.uk
EMail headoffice@consultcih.co.uk
Telephone 024 7647 2720
Registered in England and Wales: 01754648

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 Epping Forest, 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. Epping Forest's modelling: main assumptions

3.1 A model has been produced for Epping Forest launched from 2010/11 and based on the existing HRA Five Year Forecast, 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, with the exception of management costs at 0.5% above RPI)
- Roll forward of non-rent income with inflation
- General inflation (RPI) of 2%
- 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 from the original survey completed by Savills in 2004. The 30 year capital profile amounts to around £35k/unit and this is in line with benchmarks, as would be expected from the survey process that has been undertaken.

[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

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

4. Proposed settlement for Epping Forest

4.1 The headline debt settlement from the CLG for Epping Forest amounts to £164.441m. This is based on uplifted M&M allowances of 3.1%, uplifted MRA of 25.6%, resulting in a consolidated average uplift of 10.1%.

4.2 Epping Forest'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 Epping Forest, particularly high-rise. The MRA uplift is lower than the national average and the region's 31%.

4.3 The £164.441m settlement is based on a 7% discount factor. A reduced discount factor of 6.5% would give a settlement of £172.361m, a difference of £7.92m. 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 £164.441m, the debt adjustment for Epping Forest is £180.447m which is arrived at by offsetting the existing HRA 'surplus' or negative HRACFR[4] of £22.803m. This results in an 'opening self financing debt at 1/4/2011' of £157.644m. The existing differential between subsidy-debt (Subsidy CFR[4]) of £164.441m and actual debt (HRACFR) of £157.644m is therefore retained as borrowing potential within the new system for Epping Forest.

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.

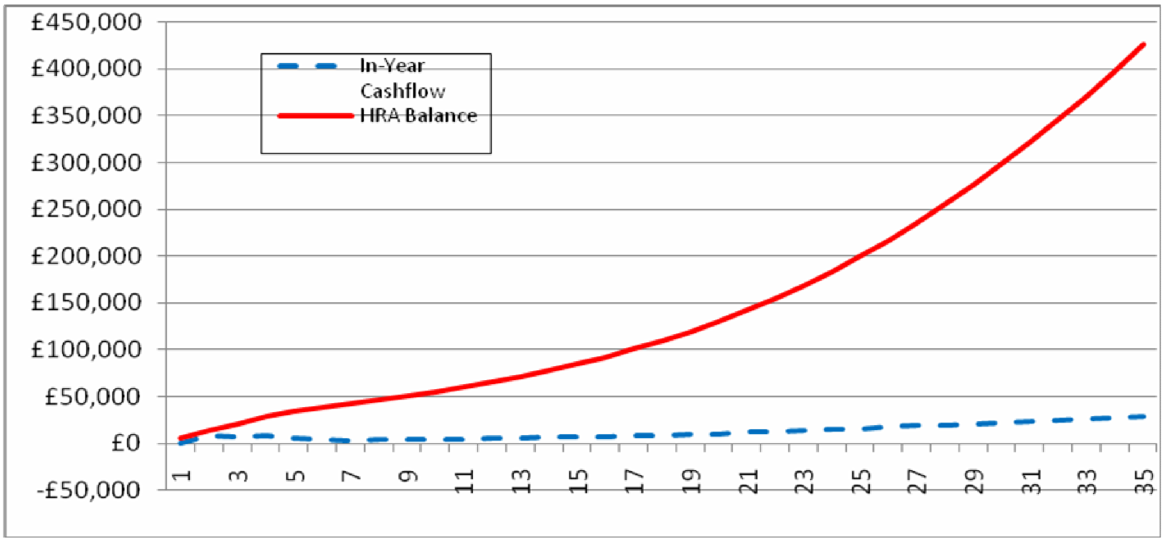
5.2 This shows that both plans are financially viable and meet all expenditure needs in each year of the 35 years covered by the plans. There is no borrowing required throughout to meet the stock investment needs over the first 10 years.

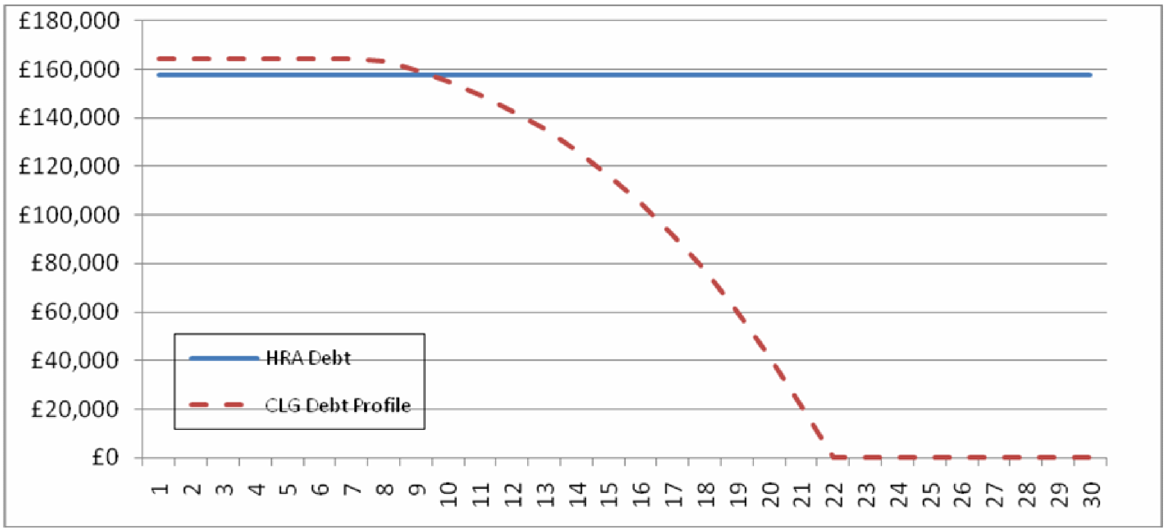
5.3 If debt is maintained as in (i) at £157.644m, reserves build to above £400m after 35 years. Charts 1a and 1b show the outcome.

[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.

5.4 If revenue surpluses are set aside to repay debt, repayment can be achieved after 18 years (compared to the CLG's assumption of 22 years) and reserves also built to nearly £450m after 35 years. Charts 2a and 2b show the outcome.

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

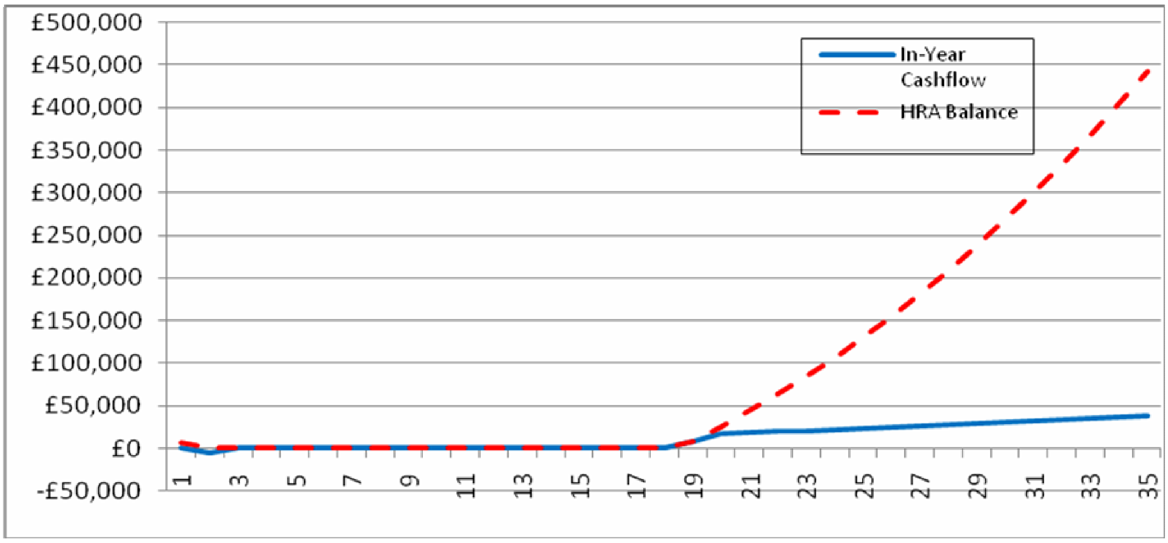


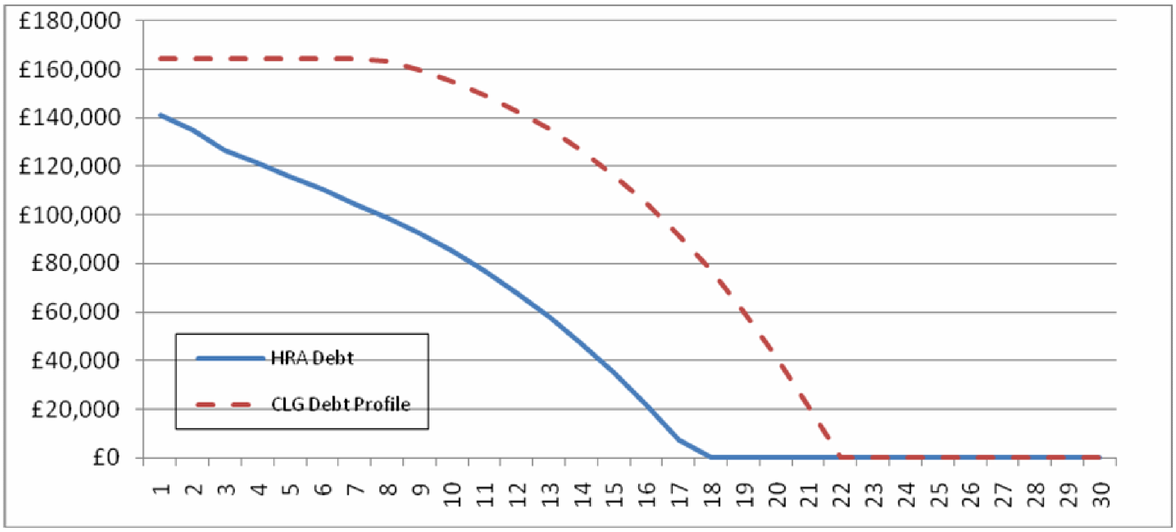


Charts 2a and 2b: Self financing revenue and debt profiles with set aside £'000

ConsultCIH Ltd
4 Riley Court,
Millburn Hill Road,
Coventry, CV4 7HP

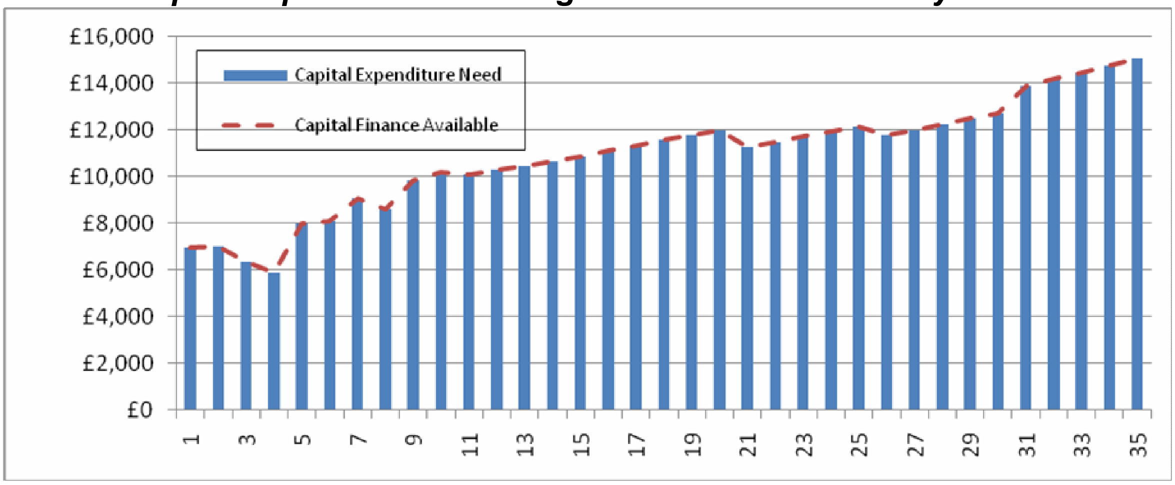
www.consultcih.co.uk
EMail headoffice@consultcih.co.uk
Telephone 024 7647 2720
Registered in England and Wales: 01754648





The Council's assessed capital investment needs, based on property surveys, are able to be met in every year of the plan. Chart 3 highlights the position.

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



6. Sensitivities

6.1 The plan is viable and resilient to changes in key assumptions. Some key headlines are set out below.

6.2 If interest rates were 7% not 6%, the debt repayment plan redeems debt by year 19 (compared to year 28). Overall the plan remains viable with considerable reserves at year 35.

6.3 Real inflation in capital costs (1% pa for 10 years) results with debt repayment pushed out to year 19. Overall the plan remains viable with considerable 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 considerable reserves at year 35and debt repaid by year 20.

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 by year 20. Overall the viability of the plan remains virtually unaffected in the long term.

7. Summary of modelling outcomes

7.1 In general, self financing based on a debt adjustment of £180.447m is viable for Epping Forest. There is in fact some room for manoeuvre for additional investment or service improvements over 30 years, given the plan's resilience as demonstrated above.

7.2 The principle reasons for the positive model for Epping Forest are:

- Rents are £7.20 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 2010/11 are £9.71m, after service charge income and non-dwelling rents, higher compared to assumed M&M (after uplifts) in the settlement of £11.34m.
- Debt begins some £6.8m 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 £11.2m

7.3 This means that although capital spending needs are £35k/unit over 30 years compared to uplifted MRA/unit of £29k/unit, there is sufficient headroom in the plan to achieve all the capital needs, subject to the sensitivities above. These could include new build and other environmental enhancements.

[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.

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 Epping Forest 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 a rate lower than the discount factor used in the settlement calculation.
- 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 capital needs, there is a capital shortfall over 30 years estimated at £105m out of a total spend of £310m (including inflation). The shortfall starts occurring after 11 years. This is based on the full investment standard, reducing this by 20% extends viability to 16 years
- The forecast HRA position is broadly in balance only for 26 years

9. Technical issues for Epping Forest

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 Epping Forest, 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 We have however identified a key issue for Epping Forest. Whilst this report concentrates on the impact on the HRA in respect of this prospectus, there will be significant implications to the Council's General Fund, as currently proposed. Currently the Council is considered as debt free overall with the following CFR position:

- General Fund £22.019million
- HRA -£22.803million
- Overall -£0.784million

9.5 As we understand under existing regulations, should Epping Forest's HRACFR change to £157.644million, the Council's standing would no longer be considered debt free with an overall positive CFR. Authorities that are not debt free are required to make debt repayments, known as Minimum Revenue Provisions (MRP). Currently for capital expenditure funded by borrowing before 2008 a 4% MRP should be applied.

9.6 In this instance the General Fund would have to make an MRP of 4%, calculated at £0.881million per annum, which it currently does not have to, resulting as additional expenditure for 2011.12 and beyond (though reducing as we assume there will be no further General Fund borrowing).

9.7 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. A 1% increase could result in additional charges to the General Fund of £0.216million per annum.

9.8 Research has identified another Council, which is in a similar position to Epping Forest, who we understand have a form of dispensation from CLG that will prevent or significantly decrease this negative impact on the General Fund. We are seeking clarification of this from CLG and will work with officers to update stakeholders throughout this period of consultation.

9.9 If, however, additional costs were to fall onto the HRA in the form protecting the General Fund in the region of £1million per annum, the resulting effect on the HRA would mean repayment of debt would extend by 2 years.

9.10 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.

9.11 We understand that the Council's Director of Finance will be providing more detailed information to Members on the effects and implications on the Council's General Fund. This is the reason that our report concentrates on the implications to the HRA and avoids covering this very important matter in greater detail.

10. Risk and reward

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

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

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 significant revenue rental surpluses will leave Epping Forest 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 £475,200 per annum. Over 5 years this, combined with 50% grant could deliver nearly 47 properties, or 235 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 30%, rents of £85 and assumed levels of repairs and maintenance we estimate that 240 properties could be provided for. 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.

11.5 We are aware of the Council's decision in principle to recommence new build for social rented housing, subject to the problems referred to earlier with the General Fund's Capital Financing Requirement being overcome. Subject to the General Fund problem being overcome, the CLG's "offer" will allow the Council to Fund a social house-building programme, through a mixture of borrowing and grants from the Homes and Communities Agency (HCA).

12. Summary national issues

12.1 The large majority of authorities, like Epping Forest, 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 Epping Forest

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

- The settlement of £164.441m results in a net debt take-on of £180.447m.
- The uplifts to the allowances to arrive at this figure are generally lower than 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
- Epping Forest could repay the debt repayment within 18 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.
- There are significant negative implications to the General Fund, however, as the Council will lose its debt free status.

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

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

- The greatest implication to the Council is the effect to the General Fund and representation on this must be made as the prospectus does state that there should be no additional burden with the adjustment of debt.
- 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.

Steve Partridge & Simon Smith
ConsultCIH May 2010