



HRA Review – Council Housing: a real future. Consultation

To: Chief Executives and housing contacts in England
For info: Contacts in Wales, Scotland and Northern Ireland

Key issues

HRA settlement proposed

Significant changes proposed

Major impacts for local authority stock retainers and ALMOs

1. Introduction

The Review of Council Housing Finance was announced in December 2007 and aimed to find a long term, sustainable system for funding council housing that would be fair to both tenant and taxpayer and fit with wider housing policy. John Healey, Housing Minister has made announcements recently and spoken in terms of dismantling the current funding arrangements. The consultation document 'Council housing: a real future – prospectus' was issued on the 24th March 2010 which is the start of the consultation period which ends on 6th July 2010.

Two significant messages emerge from the foreword. The first reflects the government's commitment to council housing as a management option into the future. Secondly the settlement is defined as a "once and for all settlement between central and local government". In order to enact this approach government may have to convince a small number of councils who do not agree with it. It is likely that most councils will wish to take advantage of the settlement but government will have to deal delicately with any that are in opposition to it.

2. Vision for self financing

The paper notes that council housing is an asset that needs strong management and investment to ensure it continues to meet people's housing needs in future which is justification for updating the financial arrangements in place, so devolving financing and accountability to local authorities. Councils will have a predictable income stream and their own rents, which they can use to maintain their own stock. The paper states councils will be able to reinvest all of their own capital receipts as part of a comprehensive asset management strategy, that all will have more to spend than they would under the current scheme and all will receive the financial independence necessary to provide an improved service to existing and future tenants. It notes that they will be able to underpin the locally driven vision for housing with a robust 30 year business plan, and then to deliver on that plan.

The paper goes on to note that if councils were prepared to take on a greater role in developing and delivering new council housing, the valuation placed on the self-financing business should reflect that. The proposal is therefore to include in the settlement some headroom to enable councils, after they have met the spending needs of their existing stock, to deliver a substantial new build programme without increasing borrowing above the opening level under self-financing. Under this lead proposal, Government would use a 7% discount rate in valuing the business, rather than the 6.5% discount rate typically used in housing transfer. This would reduce the receipt for Government from self-financing by around £1.2 billion but enable councils to deliver 10,000 new homes each year from the end of the next Parliament. The paper calls for councils to set out their ability and willingness to use this headroom to deliver new housing, so government can decide whether this is an efficient way to deliver this extra funding.

3. The settlement

The paper describes how it is proposed to calculate the income and spending needs of each council. It notes that local authorities will need to follow national social rent policy aiming for convergence. Government has not fixed a date for convergence but the model has assumed a date of 2015/16 requiring real annual increases of 2.2% in 2011 and 2.1% in each of the following four years. Under self-financing, adherence to rent policy would be secured through continuation of the limit rent and Tenant Services Authority regulation. There is also an expectation that service charges would continue to be set in line with national policy, fairly and transparently.

Recent research was carried out on the amount local authority landlords need to spend on major repairs, management and maintenance and to deal with the remaining backlog of works and the reports by BRE and HQN are published on the department's website. These reports identified a need to spend around 5% more nationally on management and maintenance and around 24% more on major repairs. The paper proposes to include these substantial uplifts to spending on management, maintenance and major repairs as part of the reforms. This will mean that self financing gives all councils more to spend on their stock as well as more flexibility to spend this money more efficiently.

The paper acknowledges that there will be some landlords who have a backlog of works needed to achieve the Decent Homes standard which will require extra capital funding in the early years. Government remains committed to completing this programme and to providing the funding necessary to do this. It recognises that £3.2bn of works are still needed to meet its Decent Homes commitment.

Under self-financing the proposal is to allow authorities to retain all their housing receipts from houses and land that fall within the HRA, provided 75% of those receipts have been or will be used for affordable housing and regeneration projects. The remaining 25% may be used for any capital purpose. Each authority with over £125,000 of housing receipts in any one year to submit a return to its auditor indicating that 75% of its housing receipts has either been spent on eligible expenditure or has been irrevocably committed to be spent on eligible expenditure. Authorities receiving less than £125,000 would only be required to submit a form signed by its chief finance officer ('section 151 officer').

The model indicates a sustainable level of opening debt for each council, based on assumptions about income and expenditure. In order to allocate the appropriate amount of debt to each local authority, an assumption must be made about the housing debt which each currently holds. The Supported Capital Financing Requirement (SCFR) figure will be used for this purpose.

Local authorities who need to borrow to make a payment to Government under self-financing will all face similar costs for that new borrowing. However, under self-financing, many local authorities will retain all or part of their existing loan portfolio and continue to charge the HRA for its share of this borrowing with varying rates of interest and it is possible that some local authorities will have a substantial amount of existing debt which continues to be charged at a relatively high interest rate. The self-financing model uses a single discount rate for all local authorities which is intended to give sufficient scope to manage their own risks under self-financing. The paper claims it isn't sensible to attempt to set a discount rate for each council which can take account of all unique local factors, including interest rates on existing debt.

A model produced by PWC which shows the level of debt that each council would be allocated is published as is a guidance document on how to use the model.

4. The financial, accounting and regulatory framework

The paper notes that the accounting, financial and regulatory framework within which councils operate self-financing must provide assurance that, under a devolved financing system, there will be sufficient safeguards for tenants and local and national taxpayers. The paper also notes that it is vital that councils develop a long term full asset management strategy bringing together revenue and capital streams of funding. The proposal is that all council landlords should maintain a council housing balance sheet setting out the assets and liabilities that support the HRA.

It goes on to say that the government sees merit in a clearer separation between HRA debt and other local authority debt, so limiting the impact business decisions in one area

have on the other. This would also provide the opportunity to eliminate complexities in the existing rules for calculating the HRA's share of debt charges.

Under the self-financing framework the paper proposes, councils would have a long term incentive to reduce debt, but no obligation to do so. They should develop a local bottom-up understanding of their housing stock, as depreciation and debt repayment will be a core part of their ongoing business planning and asset management. This approach should ensure that a backlog of capital works does not build up in future and that, if there is an identifiable need for higher levels of capital spending at a later point in the 30 year business plan, provision is made for this.

The paper notes that there is to be a cap on borrowing at the self financing debt level. Control over public sector borrowing is a high priority for government and there is a need to retain tight control over the contribution housing makes to overall levels of public sector borrowing. The intention is to propose to make a self-financing settlement that should enable most council's to fund their businesses without the need to increase local borrowing above the opening debt level set for self-financing. This is expected to be achieved via a combination of a relatively high discount rate in the self-financing valuation, higher assumptions about need to spend on management, maintenance and major repairs and a continuing capital programme to fund the backlog. Given a realistic profile for expected major repairs spend, the government thinks that this settlement should allow most councils to start to pay off debt from the first year of self-financing, creating an amount of borrowing 'headroom' up to the opening level of debt which could be used to fund new supply.

The government notes that it sees a strong future for ALMOs stating that they have experience of operating as a separate business unit and delivering major investment programmes. The paper states that it will ensure that all ALMOs who have yet to complete Decent Homes work will be able to do so with the right level of funding.

Rounds 1 and 2 ALMOs receive an ALMO allowance in the subsidy calculation, while Rounds 3 onwards have the debt added to the local authority's Subsidy Capital Financing Requirement (SCFR). The department had previously announced that after 2010-11 it will convert the allowances paid to ALMOs under Rounds 1 and 2 into supported debt. The self financing model reflects this decision by converting Rounds 1 and 2 ALMO support into debt rather than showing it as a cost allowance. This means that for these ALMOs (Rounds 1 and 2), the ALMO Decent Homes investment support allocation is not included in the costs in the model, but is covered by an increase in the level of existing notional debt against which the debt adjustment is made.

For local authorities with ALMOs, funding would be on the basis of the agreed ALMO funding and a continuation of the level of funding presently provided for Local Authority Supported Capital Expenditure (LASCE) through the regional housing pot for the planned life of the ALMO programme.

The Government expects that all ALMOs who have yet to secure funding through a 2* Audit Commission housing management assessment will achieve that performance level before self financing is introduced.

5. The HRA and the ring fence

To improve the transparency of the system, the review of council housing finance sought to identify and classify core and non-core services but it was difficult to gain a consensus around a strict definition. A third category, core-plus, was proposed to cover a range of services where there is now a general expectation that landlords will provide a service, for example on ASB and tenancy sustainment. In response to the consultation, there was almost universal support for maintaining the HRA ring-fence and for improved and updated guidance. A series of principles are proposed to enable local authorities to decide whether the service should be paid for through the HRA or the general fund. These decisions should reflect changes to Circular 8/95 and the new regulatory role of the TSA. A draft revised circular is attached to the document and is based on the following key principles:

- there should be a separate local authority landlord account that records all landlord income and expenditure (both capital and revenue) and the transfer of resources between the HRA and the general fund
- housing services that a landlord is required to provide through statutory obligations or by the TSA should be paid through the HRA
- some defined services should be paid for from the general fund e.g. housing advisory services, a proportion of the administration of a common housing register and other strategic housing functions.

The paper makes clear that transfers across the ring-fence will continue to be governed by Schedule 4 of the Local Government and Housing Act 1989, as amended.

6. Implementing reform

If local authorities wish to proceed, government proposes to work towards voluntary implementation from 2011/12, subject to confirmation at the next Spending Review. This would be achieved through existing powers in the Local Government and Housing Act 1989 (inserted by section 313 of the Housing and Regeneration Act 2008) which allow for individual agreements between local authorities and government to exclude specified housing stock from the HRA subsidy system. Such agreements would need to be in a standard form, reflecting an offer that was available to all local authorities. It would not be possible to enter into bespoke agreements based on individual negotiations. An alternative would be to implement self-financing through new primary legislation. Subject to Parliamentary time, this could be as early as 2012/13.

7. Commentary

APSE welcomes the dismantling of the subsidy system and the intention to provide local accountability and transparency in terms of housing finance. APSE has been working towards this point for a number of years and supports the approach outlined within the document.

APSE has promoted the idea of local authorities as council house builders for some time now and the current lack of supply in the housing sector justifies this argument. The move

to enable councils to build up headroom which can subsequently be invested in new homes is a positive move. However there is a danger that the target of 10,000 new council homes will be seen as an upper limit. The evidence from around the country shows that far more homes are required and councils should be encouraged to build as many properties as possible with incentives for those contributing most to the infrastructure of the nation.

APSE has noted before the impact of providing greater local responsibility at the same time as denying the opportunity to borrow. Although the paper notes allowances to meet existing maintenance and management needs, any requirement to borrow will come from those unforeseen circumstances which emerge purely from the fact that different places have different needs and circumstances. The paper promotes the concept of locality as a justification for local accountability but government must appreciate that locality means uniqueness and so avoid an approach which limits flexibility in the new arrangements. Councils are in the main financially responsible organisations but if they need to borrow, as a result of local conditions and needs, they should not be restrained from doing so. Clearly national economic circumstances will place limitations on the level of overall public sector borrowing and under current regulations local councils are subject to these limitations. However APSE has argued for a long time for a review of public sector borrowing and that the UK should fall into line with the majority of European countries and exclude investment in housing from being classified as public sector borrowing.

It would be a mistake to concentrate wholly on new build as the large majority of current properties will be with us in the foreseeable future and the maintenance and improvement of them is fundamental. This issue of borrowing is relevant here too. APSE welcomes the guidance over core, non-core and core+ services and clarification to the guidance. However there is a concern that the introduction of further classifications to meet the needs of financial rules will lead to greater confusion than is solved by the guidance.

There remains £3.2bn worth of work to be completed to meet decent homes standards and the paper notes that finding this investment will be a central element of its deliberations on investment priorities at the next Spending Review. Clearly this introduces uncertainty to the proposal and highlights the difficulties of aiming to meet a range of targets with inadequate funding. The Decent Homes programme has been widely promoted by government but it seems that success in the latter stages will depend on whether it is seen as one amongst many priorities in future discussions.

8. Consultation

APSE would encourage all members in England with housing responsibility to be prepared to contribute to this consultation process. The announcements from the Housing Minister point to this being a one off offer and it is vital that all issues are brought forward to be considered before the opportunity is missed.

9. Consultation Response

APSE will be sending a joint response to this consultation document on behalf of its members and all comments to be put into a joint APSE response should be sent by 22 June 2010 by e-mail to pbrennan@apse.org.uk. All responses to the consultation paper need to be returned by 6 July 2010.

10. List of consultation questions

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?

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