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To: City Executive Board
Council

Date: 11th September 2013
30th September 2013

Report of: Head of Finance

Title of Report: TRANSFER OF CASH AND ASSETS BETWEEN HOUSING REVENUE ACCOUNT (HRA) AND GENERAL FUND

Summary and Recommendations

Purpose of report: To seek approval to transfer assets from the HRA to the General Fund, together with a proportion of HRA cash balances.

Key decision: Yes

Executive lead member: Councillor Ed Turner

Policy Framework: None

Recommendation: That Council -

1) Transfers the non-dwelling assets identified in Appendix B with a net book value of around £18 million from the HRA to the General Fund.
2) Transfers with immediate effect, cash balances of £7 million from the HRA to the General Fund in order to fund future projects that achieve on-going General Fund savings

Appendix A – Transfer of Assets Financial Transactions
Appendix B – Schedule of assets

Background

1. Over the last few months officers have been undertaking initial work on the General Fund Medium Term Financial Plan and HRA Business Plan to review the assumptions contained within the plans agreed at Council in February 2013. In the light of recent Government announcements in regard to the Finance settlement for 2014-15 and 2015-16 and other financial pressures the General Fund Medium Term Financial Plan will be under considerable strain to continue with the delivery of its services going forward. As a result officers have been looking to identify initiatives which will create on-going savings to the benefit of the General Fund and the Council overall, whilst at the same time ensuring the continued delivery of all the Councils current priorities,with a view to reporting formally on both plans to Members in the budget round later on in the year. Two initiatives have been identified, one of which is time critical and requires approval by members before 1st October 2013.

2. This paper explains these proposals and sets out the financial implications for both the General Fund Medium Term Financial Plan and the HRA Business Plan.

3. The proposals are technical in nature and officers have been working with the Council's Treasury Management advisors, Sector Treasury Services Ltd and the external auditors; Ernst and Young to investigate the viability of:

    - Transferring non-dwelling assets in 2013/14, namely shops and garages from the HRA to the General Fund together with all the associated, management, income, expenditure, depreciation and Minimum Revenue Provision issues. This will bring certain financial benefits to the HRA and General Fund including an increase in the HRA borrowing headroom, of £17 million, equivalent to the value of assets transferred.
    - Transferring cash balances currently in the HRA to the General Fund by the 1st October 2013, to provide one-off assistance with the funding of future financial pressures in the General Fund.

4. This report sets out the advice received, processes to be followed, effect on the council's financial position and the risks associated with the transactions.

Transfer of Non-Dwelling Assets from the Housing Revenue Account (HRA) to General Fund (GF)

Power to Transfer Assets

5. The general power to appropriate (transfer) land is provided by Section 122 of the Local Government Act 1972. This provides that a principal council may appropriate for any purpose any land which belongs to them,

provided that the purpose for which it is to be used is one which they are otherwise authorised to undertake.

6. The power is subject to the land no longer being required for the purpose it was held immediately before the appropriation. In the authority's case, that purpose would be housing.

7. The land which the authority wishes to appropriate is not presently used for housing purposes but will in the past have received the specific consent from the Secretary of State to be accounted for in connection with the social housing provided by the authority in accordance with the provisions of Section 12 of the Housing Act 1985.

8. There has been encouragement in recent consultation papers for local authorities to consider carefully the items being accounted for within their HRA. In the case of such non-dwelling buildings, the benefit of usage has changed considerably since the initial accounting arrangements were approved largely as a consequence of the changes of tenancy/ownership arising from the Right to buy provisions of the 1985 Act which have resulted in the buildings no longer providing a benefit solely to the authority's council tenants. In addition a significant number of garages on council estates have been sold to private tenants

9. Section 19 (2) of the Housing Act 1985 which states that land other than that which consists of a house or part of a house may be appropriated for any purpose.

10. Like a number of authorities, including Epping Forest District Council, Corby Borough Council and Gravesham Borough Council the transfer of assets proposed in this report is predicated on the following principles:
    - Housing estates and garages are now of mixed tenure and are now no longer purely occupied by council tenants;
    - The Government's policy is that the HRA remains a ring-fenced account and should primarily be a landlord account, containing the income and expenditure arising from a housing authority's landlord functions; and
    - That the appropriations are equitable and fair to both tenants and council tax payers in the long run and provide a transparent apportionment of costs and income between the HRA and General Fund.

11. Paragraph 18.8 of the Council's Finance Rules requires full Council to agree transfers between the General Fund and HRA.

What assets are to be transferred?

12. The draft 2012/13 Statement of Accounts discloses the net book value of non-dwelling assets as at 31st March 2013 in the Councils HRA as £18.56 million. Additionally there are 4 service tenanted properties which are now administered by the HRA which it would seem reasonable to transfer from

the General Fund to the HRA with a net book value of £0.563 million. The net value of the transfer to the General Fund is in the order of £18 million broken down as follows:

		£million
a)	Other Land and Buildings	17.985
b)	Infrastructure and Community Assets	0.066
c)	Surplus assets	0.469
d)	Investment properties	0.040
e)	Properties transferred in from General Fund	(0.563)
	Total	**17.997**

13. This consists of 134 shops, 2,602 garages and parking spaces, and a number of other assets including land and substations; the details of which are included in **Appendix B.**

14. The detailed financial transactions to facilitate the transfer are set out in **Appendix A** with a summary shown in Table 1 below:

Table 1 - Summary of Financial Transactions		
Transaction	**On-going Effect on General Fund**	**On-going Effect on HRA**
	£000's	**£000's**
Garages	(657)	657
Shops	(488)	488
Depreciation	0	(417)
General Fund Dwellings	37	(37)
Minimum revenue provision	417	0
Additional Interest charges	(630)	630
Net Increase (decrease)	**(1,291)**	**1,291**

15. The credit to the General Fund and associated charge to the HRA of £630k in respect of additional interest relates to the cost of internal borrowing to the HRA..Under previous Subsidy Regulations the interest rate was based on a consolidated interest rate that charged internal borrowing at the 3 month LIBID rate, currently approximately 0.56 %. LIBID is effectively an investment rather than borrowing rate and its application has resulted in a dis-benefit to the General Fund in terms of reimbursement of costs over a number of years. Since subsidy no longer applies this anomaly should be rectified and a more realistic long term borrowing rate used. A more equitable rate would be the 25 year PWLB maturity rate currently around 4.50%. At some stage, probably in around 10 years, the HRA Business Plan will have sufficient resources to repay this debt at which time the interest credit to the General Fund will reduce.

Comments from Sector Treasury Services Ltd and Ernst and Young

16. The Council's treasury management advisors, Sector Treasury Services Ltd and the Council's external auditors, Ernst and Young have commented on the proposed transaction as follows:

- **Sector Treasury Management Ltd (Sector)**
  Sector have supported the transaction and advised on the implementation
- **Ernst and Young (EY)**
  One of the key points for EY is to ensure that 'the properties are no longer required for the purpose for which they were held immediately prior to the appropriation'. The Council's rationale is laid out in paragraph 10 above and fulfils this requirement.

Transfer of Credit Balance from HRA to General Fund

17. Schedule 4 Part III paragraph 2 (1) of the Local Government and Housing Act 1989 provides:

    "A local housing authority to whom no HRA subsidy is payable for any year may carry the whole/part of any credit balance shown in the HRA for that year to the credit of some other revenue account of theirs"

18. Whilst this clause primarily relates to those authorities that undertook stock transfer under the old subsidy system, since self-financing on 1st April 2012 no authority with retained housing stock has been in receipt of Housing Subsidy and authorities are able to use this provision to transfer credit balances from the HRA to the General Fund.

19. The proposal is to transfer a sum of £7 million from the HRA to an earmarked reserve in the General Fund to be used on projects to create on-going future financial benefits.

20. Advice from the Head of Law and Governance indicates that Schedule 4 Part III paragraph 2 referred to above will be amended on 1st October 2013 by virtue of the Localism Act 2011 (Commencement Order No 9) such that it will no longer be in force in England (but will in Wales). Any cash transfer must, therefore, take place prior to the 1st October 2013.

21. Officers have sought the views of both the Council's treasury management advisors, Sector Treasury Services Ltd and external auditors, Ernst and Young who have advised the following :

- **Sector Treasury Management Ltd**
  Sector have referred to the Local Government and Housing Act 1989, Schedule 4, Part III, Paragraph 2 which the Council is relying on to make the transfer and advised that in their opinion the Council may rely on this clause to effect the proposed transfer.
- **Ernst and Young**
  The Council's auditors have advised that they are 'not minded to challenge the statutory basis for the proposed transfer'.

Financial Implications on General Fund MTFP and HRA

22. Whilst a full refresh of the HRA Business Plan will be undertaken and submitted to Members as part of the Budget Process in December some initial work has been undertaken to update key assumptions included within the Plan agreed by Council in February 2013 to determine the impact on the HRA of the proposed changes. Key assumptions updated include :
    - **Rent increase –** the original plan assumed a rent increase in accordance with the rent convergence formula i.e. RPI+0.5%+£2, (RPI being 2.6% in September 2012) with convergence expected in 2018. However recent announcements from DCLG suggest that the rent convergence element of the formula, (the additional £2) will be scrapped and that inflationary increases of CPI+1% will be applied from 2014/15 rather than the current RPI + 0.5%. The updated HRA Business Plan assumes CPI at 2.1% (average CPI since 1997) i.e. rent increases of 3.1%. This change reduces on-going rental income in the Business Plan by around £600k per annum, although clearly this could change depending on the way CPI is calculated and its future level.
    - **Property disposals** –Based on 9 right to buy disposals to date, the figure allowed for in the plan has been reduced from 78 per annum to 20 per annum.
    - **Bad Debt provision –** The bad debt provision in the original business plan is considered overly prudent with arrears at less than 2% of the debit. The provision has therefore been reduced from £0.5 million to £0.4 million.
    - **Tower block refurbishment program** changed from £10 million spread over 8 years to inclusion of a budget of £16 million with completion of the programme in 4/5 years**.**
    - **New build-** The authority made provision within the original business plan of £60 million for new build housing. The latest projection of spend on new build, primarily Barton, is £38 million for the purchase of approximately 350 properties.

23. In addition the following assumptions continue to be allowed for in line with original assumptions;

    - The removal of the service charge limiter by £1 per week.
    - Efficiency gains on capital works and responsive repairs by Direct Services.
    - The delivery of 112 new build dwellings under the Affordable Housing Program.
    - The continuation of the adopted policy on self-financing debt redemption.

24. Table 2 below reflects the impact on HRA balances of the asset transfers highlighted in para 12 above,a one-off transfer of £7 million using the

provisions highlighted in para 17 above and the assumptions as set out in paras 21 and 22 above. The plan indicates that both transfers can be undertaken without materially impacting the HRA's strategic objectives and maintaining balances at a prudent level in excess of £3.5 million.

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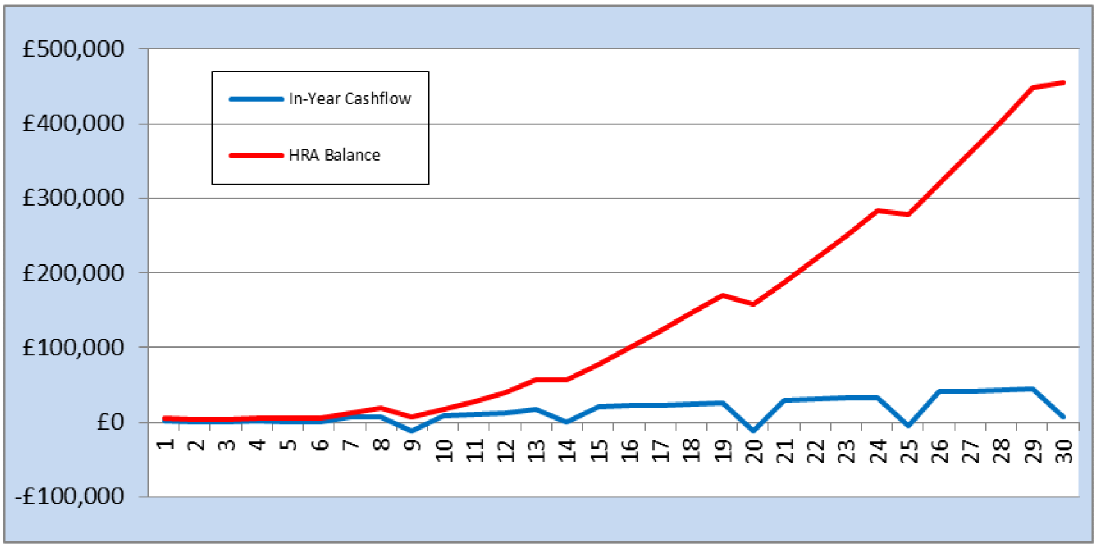
Table 2 - Summary of HRA Working Balances					
	2013/14	**2014/15**	**2015/16**	**2016/17**	**Total**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Original Business Plan	5,670	4,459	9,074	5,944	25,147
Revised Business Plan	3,534	3,619	4,837	5,036	17,026
Variance	**2,136**	**840**	**4,237**	**908**	**8,121**

25 In the longer term these changes in the working balances escalate over the 30year period after year 9 following completion of the Barton scheme which is illustrated in the graph below :

£'000's



26 The graph indicates that HRA working balances (the top line) will rise to around £450 million by year 30 having completed all current new build housing schemes in the programme, ongoing annual refurbishment of existing council dwellings of around £7 million per annum, tower block refurbishment and repayment of approximately £120 million of debt repayments.

Increase in HRA Headroom

27 The transfer of assets proposal (£18 million) creates an equivalent increase in the HRA borrowing headroom. The Council currently has borrowing headroom of £19 million. Rules governing appropriation of assets requires an adjustment to the HRA Capital Financing Requirement hence borrowing headroom will increase to around £37 million. This will give the council additional opportunity for capital investment in its housing stock meeting the objectives of the housing strategy. This could include:

- Up to 350 new build council houses
- Retrofitting of existing stock with energy improvements to reduce tenants energy costs and increase fuel efficiency
- Expansion of the Council's Great Estates program
- Creation of an Oxford Homes standard beyond Decent Homes
- Extensions to void properties to help meet overcrowding need

Implications for the General Fund Medium Term Financial Plan

28 A full refresh of the Council's Medium Term Financial Plan will be undertaken and submitted to Members as part of the Budget cycle in December, initial work has been undertaken on updating several key assumptions included within the Plan presented at Council in February 2013, to determine the implications of recent Government announcements and the financial effect of the proposed changes.

29 Changes to original assumptions include:

- **Revenue Support Grant** -Taking account of the changes to Revenue Support Grant (RSG) on which the Government is currently consulting for 2014/15 and 2015/16 and reducing RSG to zero in equal instalments between 1/4/2016 and 1/4/2020.
- **Blackbird Leys Pool** -Deferring the management saving on the pool by 6 months as a consequence to the late start on site
- **New Homes Bonus** -Top slicing New Homes Bonus by 20% from 2015/16 and deleting New Homes Bonus and Revenue contributions to capital by 2017/18, the final year for which the first round of NHB was guaranteed
- **State Pension Changes** - Inclusion of additional £400k per annum from 2016/17 being the estimated financial implications associated with the proposed second state pension changes in 2016.
- **Council Tax** - Increasing Council tax by 1.99% for 2014/15 and 2015/16 from 1%.included within the original plan
- **Contingencies**- contingency adjustment to allow for savings achieved in 2012/13

30 The above changes give rise to a shortfall in the Medium Term Financial Plan of around £1.8 million in 2015/16 rising to a £6.5 million on-going deficit by 2020.

31 The transferring of assets outlined above would improve this position by around £1.3 million on-going. The transfer of the £7 million would need to

be applied so as to create on-going revenue savings to the Council in a similar manner to the transfer of assets. Officers are currently looking at a number of proposals to achieve an ongoing saving to the General Fund.

Financial Implications

32 The proposals set out above for the asset transfers and cash transfer between the HRA and the General Fund are legal and financially viable for both the HRA and the General Fund. Whilst there is an opportunity cost to the HRA it is important to note that the Housing Revenue Account can still meet all the Council's current strategic Housing objectives.

33 The transactions improve the Council's overall financial resilience, facilitate the protection of services and are therefore of benefit to all residents of the City.

34 An added value of the proposals is that due to the accounting arrangements there is an increase in the head room for HRA borrowing by an amount equivalent to the value of the transfer of around £18 million, effectively doubling what the Council already has. This will provide additional resources to the Council and enable it to undertake works to the benefit of the HRA suggested in paragraph 27 above.

Legal Implications

35 These are set out within the body of the report

Equalities Implications

36 The proposals will be of benefit to council tax payers in Oxford City and will help safeguard jobs and services provided by the General Fund.

Risk Implications

37 There is a risk that DCLG will introduce legislation retrospectively to repeal Schedule 4 Pat III para 2 from 1st April 2013. In this instance the Council would not have the power to transfer the HRA cash balances (£7m) as proposed.

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Background papers: None

APPENDIX A

FINANCIAL EFFECTS OF THE TRANSFER OF ASSETS FROM HRA TO GENERAL FUND

Transaction	On-going Effect on General Fund	On-going Effect on HRA	Note
	£000's	**£000's**	
Garages			
Income	(974)	974	1
Planned Works	143	(143)	
Garage Management Team	174	(174)	
Shops			
Income	(634)	634	2
Planned Works	91	(91)	
Shops Management Team	55	(55)	
Depreciation non-dwellings	0	(417)	3
General Fund Dwellings			4
Income	40	(40)	
Revenue Repairs	(3)	3	
Minimum revenue provision	417	0	5
Interest charges	(600)	600	6
Net Increase (decrease)	**(1,291)**	**1,291**	

Notes

1 We have a stock of 2,602 garages that generate annually rental income of approximately £0.974 million.
2 There are 134 HRA commercial shops that generate annually rental income of £0.634 million.
3 Accounting convention requires a charge to be made to the HRA for depreciation based on the valuation of the asset and its useful life. Transferring assets to the General Fund will result in a saving to the HRA in respect of depreciation in the order of £417k and since depreciation charges are reversed out in respect of general fund assets there will be an overall saving to the Councils revenue position of the same amount.
4 There are 4 dwellings with a value of around £500k currently accounted for in the council's General Fund. These relate to previous service

tenancy properties at various depots and cemeteries etc. It is considered that these, as they are now managed by Tenancy Services within the HRA, be transferred to the HRA i.e. appropriated the other way to the proposed garages and HRA commercial property transfers.

5 Minimum Revenue Provision. - Accounting convention requires the Council to set aside an amount from revenue for the repayment of debt based on its MRP Policy set out in its Treasury Management Strategy which charges MRP on new capital expenditure, where financed by Prudential borrowing, based on the estimated life of the asset being purchased. Prudential borrowing increases the Councils underlying need to borrow for capital purposes, known as its Capital Financing Requirement (CFR). Whilst there is no overall increase in the CFR, simply a change between the HRA and the General Fund CFR, it is up to the authority to decide on the amount of MRP to charge.

6 Interest charges on internal borrowing– The HRA has internal borrowing (the difference between actual debt and underlying need to borrow for capital purposes or CFR as it is known, of around £24 million. This is currently being financed by the General Fund and has remained unchanged following self-financing. Under previous arrangements there was a statutory requirement for the amount of interest charged to the HRA for this borrowing to be calculated using a consolidated interest rate that included an element at the 3 month LIBID rate, currently approximately 0.56 % which has resulted in a disbenefit to the general fund in terms of its reimbursement of costs over a number of years. The 3 month LIBID approach was recognised by CIPFA as wholly inequitable when considering the manner of accounting for loan interest costs. The reason being that just because the authority happens to decide to finance internal borrowing from its own resources for a temporary or longer term period, the HRA should not necessarily benefit from this from an artificially low interest rate being used. Accordingly it is suggested that the amount of General Fund investment income earned in respect of this £24 million loan to the HRA should be at a more equitable long term borrowing rate currently around 4.53%, 25yr PWLB Maturity rate.

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