Annex 1

North Tyneside Council

2013-2015 Financial Planning and Budget Process:

Cabinet's Final Budget Proposals for the Housing Revenue Account (HRA) Business Plan and Budget for 2013-2015
16 January 2013

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Section 1
The 2013-15 Financial Planning and Budget Process

1.1 Introduction

As Cabinet will be aware, following on from last year's budget process and subsequent Counsel's opinion, this meeting is being asked to receive and approve the Housing Revenue Account (HRA) budget for 2013/14. As part of that process Cabinet are being asked to set the rent increase, along with the garage rent and service charge increases and the 2013-2023 Capital Plan.

Cabinet will also be aware that 2012/13 was a year which saw the introduction of self-financing HRAs and the abolition of the HRA Subsidy system. These were the biggest changes to housing finance in decades, and were introduced under powers enacted by the Localism Act 2011 from 1 April 2012. The essence of the change is that in future this authority will keep all rents raised locally and will no longer have to pay over any sums to Government. In addition there is an assumed average increase in the amount of money estimated to be spent on major repairs, management and maintenance costs.

The "price" of this increased local determination was a one-off national debt adjustment, which redistributed over £20 billion of council housing debt held nationally, of which this authority's share was finally determined to be £128.193m. This sum was borrowed from the Public Works Loan Board (PWLB) on 28 March 2012 and paid over to the Treasury. In addition the Authority will also be exposed to future inflationary and interest rate risks, from which it was previously protected to a large extent by the subsidy system. This makes future efficient use of resources and Treasury Management decisions in relation to the HRA of paramount importance, and these will also be discussed as part of this report.

The key principles of the new self-financing proposals were explained in the Cabinet Report "Housing Revenue Account Self-Financing" (28 November 2011). This report and last year's budget report set out the implications of the major decision areas recommended in that report, and the implications for the Financial Planning and budget-setting process for 2012/13 and beyond, in particular the assumptions made in relation to the Government's policy on rent restructuring, the treatment of new and existing debt portfolios, and the future investment needs of the stock in capital terms. These issues are revisited in this report to analyse the continued implications of self-financing as we move into the second year of the new system.

This report also analyses the potential implications for the HRA of further significant changes which have occurred and are still in the process of occurring, namely:

- Welfare Reform changes with particular reference to the impact on tenants and the resources they have to manage their budgets. The introduction of a charge for under-occupying tenants from April 2013, and the potential introduction of the

Universal Credit from October 2013 with direct payments for most tenants may create significant resource issues for some of our tenants, and for the Authority as it seeks to maintain efficient collection of rental income;

- Right to Buy (RTB) – the announcement last Autumn of a significant increase in the maximum discount available to Council tenants by Government, coupled with the start of a national advertising campaign is sparking some revived interest in the RTB option for our tenants. The self-financing model assumed a relatively modest level of RTB over the next 30 years, if, as a result of this policy change, sales outstrip those projections this could cause resource problems for the HRA.

This report also sets out the efficiencies, financial and service pressures on the HRA which have been identified through the financial planning process. Cabinet will wish to take these into account when it considers the HRA financial plan for 2013/14 to 2014/15 and the associated 30-year Business Plan.

The budget proposals also incorporate the commencement of a programme of new build Council Housing, which will see the start on site of the first Council homes to be built in the borough for nearly 25 years.
These proposals were outlined and approved by Cabinet following the 13 August 2012 report "Building Council homes". Additional year-end revenue balances identified in 2012/13, along with New Homes Bonus contributions, and the use in 2013/14 of Capital Receipts from RTB and other land sales, and the expected 2012/13 savings which will come via the House-building Fund from Treasury savings in relation to the self-financing loan deal (following external audit approval of 2012/13 Final Accounts), have enabled the Authority to commence preparations for two separate schemes at Station Road and Byrness Court, in advance of the originally identified start of a new build programme in 2014/15.

Cabinet will be aware that a long-term view of the HRA financial position is regularly taken. For the purposes of the current Financial Planning and Budget Setting process a two-year plan has been developed in line with the approach adopted for the General Fund as is outlined below, to reflect the two years that remain in the Government's current Spending Review (SR) period. Cabinet is advised that the second year projections are only indicative at this stage. As part of the self-financing process the authority has continued to develop its 30-year plans to ensure the long-term viability of the HRA.

Historically the HRA budget-setting process has always revolved around the issuing of the Subsidy Determinations each year, which have had a major impact on the HRA budget. In particular items such as subsidy due or repayable, amounts available to support capital spend, capital charges incurred by the account and rent increase levels under the rent restructure formulae were set based on information and requirements outlined in the determination. With the introduction of self-financing this has all changed. In previous years subsidy determinations have appeared in draft in December, with final ratification received in January, which has made financial planning far more difficult. From 2012 onwards, , the critical determinants will be the decision on the level of rent increase and the amount of rent the Authority collects, the Treasury Management Strategy used to manage our debt portfolio, how costs are controlled for managing and maintaining stock and the future investment needs of that stock.

As in previous years, setting the rent will be a crucial element of the HRA budget-setting process. The introduction of the HRA self-financing regime included an assumption by Government that all authorities would continue to follow the national Rent Restructuring policy, which assumes convergence for most properties in 2015/16. Not following that policy would have significant implications for the HRA in terms of the level of resources available to manage, maintain and develop the existing stock, and any opportunity to develop new stock. Hence, one of the critical determinants in the budget process becomes the Retail Prices Index (RPI) figures for September each year (announced mid-October), which form the basis of the formulae for calculating the rent increases required.

For 2012/13 the RPI as at September 2011 was 5.6% which resulted in an average rent increase of 9%. As explained below the RPI for September 2012 was 2.6%, which will see a recommended average increase for 2013/14 of 5.81%. As a result of this, financial planning for the HRA can be applied with some degree of increased certainty.

The following budget proposals include the impact of all the key determinants of the budget referred to above, and their impact on the HRA business planning process. Cabinet should be mindful that, given the nature of the significant changes in policy that have been implemented nationally, and further changes which are being implemented, the Authority continues to closely monitor the position of the HRA due to the number of variables impacting over the coming years.

Section 2
Strategic Planning

2.1 Decent Homes Standard Progress

The 2012/13 HRA budget including the Business Plan and 2012-2022 Housing Capital Plan, which were approved by full Council as part of the 2012-2015 Financial Planning and Budget process, allowed for the Decent Homes Standard to be maintained for most of the General Needs Housing and non-traditional build properties owned by the Council.

The Department for Communities and Local Government (CLG) approved a draft allocation of Private Finance Initiative (PFI) credits totalling £110.400m for the redevelopment and refurbishment of the authority's Sheltered Accommodation units following the successful submission of the Outline Business Case for the Quality Homes for Older People project. The Authority is now in the process of evaluating the bids of the final two tenderers following the call for Final Tender, and should reach financial close and start on site by the middle of 2013. The projected revenue and capital implications of the successful PFI approval have been included in these budget proposals. The project has been and continues to be rigorously reviewed for Value for Money by HM Treasury, and is still the Authority's best solution to bring all of our homes up to the required Decent Homes Standard.

2012/13 was the first year of a post-Decent Homes Programme under a self-financing environment. The over-riding future objective is to ensure that the housing stock is, as a minimum, maintained at Decent Homes Standard (DHS). The Asset Management Strategy was agreed in the "Better Homes – Better Lives" 2010-2015 report, which was approved by full Council on 9 September 2010. In that report full Council approved a new stock condition survey to be undertaken and used to update the assumptions within the Capital Plan to ensure that the future needs of the stock are fully met. This survey was completed, and the results were fed into the Authority's Keystone Asset Management system.

As with the rest of the HRA Business Plan these figures need to be constantly updated, to reflect the identified needs of the stock, and to, where possible, build in the identified key priorities of our tenants represented via the Tenant Panels. The implications of the survey work along with the outcomes of the consultation processes, and identified resources have been fed into an updated Capital Plan and this estimates the capital need over the next three years will total £49.806m, with £1.209 billion needed over the next 30 years, excluding any assumptions on new build.

If the assumptions outlined in this report are agreed by Cabinet in setting the HRA rent and budget for 2013/14 and beyond, then there is the potential for an estimated 810 new homes to be built over the next 30 years, providing the HRA can identify enough suitable land and there are no significant changes in the key assumptions within the plan. This estimate is based on the average price of a 3-bedroomed property. Given the identified need for one and two bed-roomed properties tied to the Welfare Reform changes, it is possible that the Authority could build more than 810 properties.

These assumptions in relation to the Capital Plan are fully reflected in the budget proposals outlined in this report.

The Council's Joint Venture partner (Kier North Tyneside Limited) will deliver the majority of the works identified as required to the current stock within the Capital Plan up until at least 2019, as is necessary to maintain the stock at the DHS. The funding assumptions on capital reflect current issues around a need to review our HRA-owned land stocks.

As agreed previously by Cabinet, the plan assumes that a proportion of any Right to Buy (RTB) receipts over and above those assumed for self-financing, will be set aside to repay debt rather than finance capital; this will help to mitigate against viability issues for the HRA business plan which may arise under the changes introduced by the Government to reinvigorate the Right to Buy scheme by increasing the maximum discount to £75,000. Any set aside will be subject to the restriction that the Authority will have to comply with the new RTB agreement signed with the Government committing the Authority to use any additional receipts to fund new build. Given the Authority's proposed new build programme, this should be deliverable as it is anticipated that the Authority will be able to match spend to any targets.

In terms of the self-financing HRA Business Plan, 2013/14 represents the most difficult year in terms of available Capital resources. The proposed total Capital programme for 2013/14 excluding new build works, but including currently identified re-programming from 2012/13 totals £15.187m. This compares to the last year of the Decent Homes Programme in 2010/11 which saw £35.699m of capital works being delivered, of which £21.510m was funded from Prudential Borrowing.

Under the proposals for self-financing, part of the deal in determining the debt settlement for the authority was to provide for an increase in the level of funding available for major repairs. This, coupled with a steady increase in the level of revenue contributions available after 2013/14, makes it possible to plan for the long-term to ensure that not only are all existing stock needs met, but that the Authority can, subject to compliance with Central Government Policy, put itself in a position to begin building new council houses from 2012/13 onwards. Further details on the Housing element of the Capital Plan and capital financing arrangements are included in Section 4.0 of this annex.

2.2 HRA and Treasury Management issues following the Self-financing Debt Settlement

The HRA is a separate landlord account that reflects revenue expenditure and income relating to the Council's own housing stock. It is an account that is ring-fenced from the Authority's General Fund with statutory guidance about the items that can be charged and credited to it. The Authority has a legal duty to prepare budgets that ensure that the account remains solvent and to review the account throughout the year.

Formerly each authority's HRA was part of a national housing subsidy system whereby authorities which made a surplus on their "notional" HRA account (calculated using Government assumptions) made payments into a central pool. This was then used, amongst other things, to subsidise authorities that made a loss. In the last few years of the subsidy system North Tyneside was a net payer of housing subsidy, with actual payments of £7.089m for 2011/12 (budgeted £6.141m). These payments were projected to continue to rise significantly year-on-year if the current subsidy system had remained in place.

From 1 April 2012 each authority retains all rents raised locally, and is no longer required to make or receive any subsidy payments to or from central Government. This change was achieved via a "one-off" re-allocation of debt. In effect each authority either bought itself out of the system, or was bought out of the system. The debt settlement figure was calculated by determining the commuted Net Present Value (NPV) of expected future income and expenditure streams for the next 30 years. This value was then compared to the HRA Subsidy Capital Financing Requirement (CFR), and if the NPV figure was higher, the difference between the two figures was the additional amount of debt an authority had to take on. If it was lower the authority would get some or all of its debt repaid.

The final NPV figure for North Tyneside Council at 31 March 2012 was £270.585m, which was £128.193m higher than the subsidy HRA CFR of £142.392m at that point, and hence that was the amount of additional debt that was allocated to this authority. The overall CFR of the authority will be used to "cap" any future borrowing. This authority had a subsidy HRA CFR of £142.392m at 31 March 2012, but an actual HRA CFR of £162.631m. This difference is because the authority had to borrow significantly to finance the Decent Homes Programme. The Government has agreed that any authority with an HRA CFR that exceeds their subsidy CFR will have their "cap" adjusted to reflect the higher figure to avoid the Authority immediately exceeding the cap.

Table 1: Final Calculation at 31 March 2012

Calculation	**£000's**
NPV Figure	270,585
Proposed Initial HRA Debt "Cap"	270,585
Subsidy HRA CFR	142,392
Additional Debt	128,193
Notional Total HRA CFR	270,585
Actual HRA CFR	162,631
Additional Debt	128,193
Actual HRA CFR	290,824
Revised HRA Debt "Cap"	**290,824**

Hence, £290.824m was the starting point for the total amount of debt that the HRA will have to manage within the business plan over the next 30 years. So, although the Authority will no longer have to pay subsidy, interest and principal repayment costs (depending on the repayment strategy) will be paid on £290.824m of debt. Cabinet and full Council chose to follow the recommendations of the Cabinet report "Housing Revenue Account Self-financing" (28 November 2011) in relation to the strategic treatment of the overall debt. The Authority agreed to follow the Chartered Institute of Public Finance and Accountancy's (CIPFA), recommendation that the Authority treats the HRA as having a separate debt pool from the General Fund. There are three distinct elements to this:-

1) **Self-financing debt** – The £128.193m payment to the Government was funded by taking out a total of 25 separate loans for £5.000m each, and one loan for the balance of £3.193m with maturity periods ranging from 24 to 50 years. These loans are directly attributable to the HRA, and will be managed as such. The loans were financed with long maturity periods because the interest rates being offered by PWLB for self-financing were at a "one-off" premium" against what were already historically low interest rates. Hence, it made prudent financial sense to finance these sums long-term. The average interest rate achieved on these loans totalled 3.49% which equates to an annual interest payment of £4.477m. This is an estimated £0.652m below the figure budgeted for 2012/13, and this sum, once ratified, will be transferred to a House-building Fund. The funds accumulated in this Reserve have then been agreed to be used to fund the new build programme as identified in the August 2012 Cabinet report, and the Capital proposals contained within this report;

2) **Existing Debt** – The Authority has already established that the HRA has a share of the pre-self-financing debt portfolio valued at £162.631m as at 31 March 2012. In order to create a separate portfolio of existing debt for the HRA, each long-term existing loan was split proportionally with the General Fund. This means that at the point that each loan reaches maturity, there is a separate consideration for both the General Fund and the HRA as to whether they would wish to re-finance their share of the loan, either long-term or short-term, or whether they would wish to use debt set aside to effectively repay the debt. The HRA self-financing strategy agreed by Cabinet is that where possible it will seek to repay these existing loans where prudent and affordable. Hence, there may be the opportunity to undertake short-term borrowing at rates around 0.25% to 0.35% when loans reach maturity, which may enable some additional short-term savings to be made, assuming that those rates remain at existing levels. These have been identified in the HRA Treasury Management Plan, and built into the financing assumptions for the HRA Business Plan. For 2013/14 it is estimated that the total interest payments due on the existing debt portfolio will total £8.470m, with a debt set aside of £3.900m; and

3) **New HRA Debt – short-term and long-term**, As already described, any new borrowing that the HRA undertakes, whether that be re-financing of the HRA share of existing loans, or genuine new borrowing (currently restricted because of the debt cap) will be made through new loans which

will be easily attributed solely to the HRA. For 2013/14 there will be re-financing of £9.946m of loans, and some temporary borrowing which in total will cost £0.136m in interest charges to the HRA.

Therefore, over time the authority will build a separate portfolio of HRA debt, with differing strategic considerations to the General Fund. For 2013/14 the overall impact of the recommended debt portfolio approach, will be a total estimated interest charge of £13.083m and a set aside cost of £3.900m included in the total estimated financing payments of £16.976m for 2013/14. This can be compared to the original budget for 2012/13 where the estimated interest costs totalled £14.053m, and set aside was £2.500m, with an estimated overall cost of £16.553m. Currently it is being predicted that the actual costs for 2012/13 will be in the region of £15.624m realising a significant saving.

These costs are now exposed to interest rate risks in the market, but in the current climate represent the best estimate of the implications going forward. Although the HRA has taken on significant additional debt, close control over the costs associated with that debt will realise true benefits to the HRA over time, compared to a subsidy scenario where the contributions to Government were rising exponentially year on year.

The HRA is restricted by the imposition of the debt cap at £290.824m. The Authority's total borrowing cannot exceed this figure at any future financial year end. However, North Tyneside Council are in a small group of authorities for whom this rule will be flexed, and that is due to the Authority's Quality Homes for Older People Private Finance Initiative (PFI) Scheme. Once the scheme reaches financial close, there will be a build period of up to approximately 4 years (depending on the successful preferred bidder), which will incur significant capital costs. These costs have to be recognised in the Authority's Capital Financing Requirement (CFR), hence if the Authority was not allowed to break the cap to reflect the Capital spend, the Authority would be in breach of the self-financing regulations. North Tyneside Council have sought and had written assurance from the Department for Communities and Local Government (CLG), that they will work with us to ensure that the cap is flexed appropriately to reflect this. This is effectively a technical adjustment, and the cap will reduce over the 28 year life of the scheme, as the debt is notionally written down.

The Authority will continue to monitor closely the Treasury Management position and the potential impact on the HRA, and consult closely with the Elected Mayor and the Cabinet to ensure that the best results are achieved for the HRA and our tenants. The current approach taken to Treasury Management reduces the re-financing risks attached to the business plan, and also provides some flexibility in terms of future investment and potential additions to the stock.

The proposed HRA Treasury Management Strategy for 2013/14 is attached as Appendix C to this report. This has been updated to reflect the implications for the Treasury Management Strategy of the Housing Self Financing Settlement. The key elements of the Strategy are:

- Treasury limits in force which will limit the treasury risk and activities of the Authority;

- The current treasury position;
- Prospects for interest rates;
- The borrowing strategy;
- Interest risk;
- Policy on borrowing in advance of need;
- Debt rescheduling;
- Annual investment strategy;
- Monitoring credit ratings; and,
- Policy for the use of external service providers.

Treasury Management continues to be affected by on-going economic uncertainty with low returns on investment and low short term borrowing rates. The expected longer run trend for Public Works Loan Board (PWLB) borrowing rates is for them to rise slightly during 2013/14 with the bank interest rate expected to remain constant at 0.5%.

If interest rates were to rise then rates for investment would also increase and the Authority would benefit from improved investment returns on any cash surpluses it holds, after taking into account the primary requirement to safeguard the Authority's assets. Movements in both short and long term interest rates are monitored on a daily basis to try and gauge the best lending and borrowing options for the Authority.

2.3 Self-Financing and Depreciation

As part of the proposals for self-financing CLG declared a desire to ensure that authorities make proper provision for the future investment needs of the stock and they aim to achieve this by introducing a true charge for depreciation. As explained in the "HRA Self-Financing" Cabinet Report, the Major Repairs Allowance (MRA) is currently used as a proxy for depreciation, with any revaluations and impairment charges being reversed out of the accounts; the same principle is applied to the General Fund.

A true depreciation charge could make the business plan unsustainable, which is of major concern to all stock-owning councils. There is also a requirement to assess the different components of assets with differing lifecycles (e.g. kitchens and bathrooms), under International Financial Reporting Standards (IFRS), which could also lead to variations in depreciation charges previously used.

To allow time for further work to be undertaken to resolve this and consultation with CIPFA, CLG established an interim solution; to allow an up-rated MRA figure to be used as a proxy again for up to five years whilst a workable long-term option is developed.. This budget assumes that the Authority will move towards calculating a true depreciation charge, but will continue to use the MRA proxy as a fall-back position for up to five years, whilst this issue is resolved fully.

In terms of using the proxy MRA figure for 2013/14 this means that the transfer to the Major Repairs Reserve that will be required in 2013/14 will increase from £13.418m to approximately £13.610m. As outlined in the self-financing report, there are two elements to the MRA charge. Because our Quality Homes for Older People project had not reached financial close before self-financing was introduced, our debt settlement was based on the stock including the PFI properties. This means that the debt we took on was reduced by the MRA attributable to the sheltered properties.

To take account of this when the deal is signed, our PFI credits will be reduced by the amount of MRA attributable to the PFI properties as at 31 March 2012 (pro-rata for the first year). To compensate for this we need to make an accounting adjustment in the MRA calculation. The adjustment required will be approximately £0.798m of MRA in a full year, which will be fixed for the 28 year term of the scheme, and will not be subject to inflation. For 2013/14 the Council has estimated a charge of £0.599m will be provided from MRA, with a further increase of £0.199m in 2014/15.

The sums that are transferred to the Major Repairs Reserve to reflect depreciation can only be used to either pay off debt or fund major repairs and cannot be used to balance the HRA business plan.

2.4 Rent Restructuring

As mentioned in the introduction to this report, the self-financing HRA system which has replaced subsidy continues the Government's current policy assumptions in relation to rent restructuring. Hence, Government sets a "guideline" rent that the Government assumes authorities charge to their tenants. This guideline rent is set according to Government policy on rent restructuring. The objective of rent restructuring is that similar affordable rented homes in the same area should have similar rents regardless of who the landlord is, and therefore deliver more consistent rents and greater transparency for tenants. It will also ensure that that landlord has sufficient resources to maintain its homes to the decent homes standard as a minimum. Under this policy, properties with lower or higher rents than a Government set formula have their rents progressively increased or decreased (in the case of Housing Associations) each year until they reach the Government's target. Individual rent increases are limited to Retail Price Index (RPI) + 0.5% + £2 (per week).

Authorities can set rents below this level, but they will have to be able to afford the reduced rental income in their overall HRA. The rent restructuring policy was introduced in 2001/02 and originally required the rent for all Local Authority and Registered Social Landlord homes to reach their "formula rent" target level by 2011/12. This was referred to as "convergence" as the intention was for local authority rent levels to converge with the higher rents charged by housing associations.

In recent years the Government has amended the rent restructure formula to allow authorities to reduce the rent increase in part by adjusting the rent convergence deadline and consequently the guideline rent increase. This has had a direct impact on the rent increase now required through the rent restructure formula. For 2011/12 the Government compensated those authorities where the rents were "constrained" from their full convergence path because of the maximum "cap" limit.

For North Tyneside Council this compensation equated to £2.73 per property per week in 2010/11, which was taken into account in determining the 2011/12 Subsidy payment. Under self-financing the Government have built-in an average level of compensation for each property and this was reflected in the debt settlement figure. This means that using a global average will disadvantage those authorities with a high level of compensation and means that not every property will converge by 2015/16.

The self-financing proposals already discussed assume that all authorities will continue to implement rent restructuring with a "convergence" deadline of 2015/16. Hence, the financial model that the Government developed to calculate our debt settlement assumed that the Authority's rent increases would continue to mirror the rent increases reflected in that model. If they do not, the Authority will have problems generating the resources required to make the business plan balance and meet the future needs of the existing stock.

The rent restructuring formula for 2013/14 is based on the RPI level prevailing at September 2012 as a base. No individual weekly rent should increase by more than RPI + 0.5% plus £2, which allows authorities the scope to narrow the convergence gap. The RPI prevailing at September 2012 was 2.6% compared to 5.6% in September 2011. Applying the rent restructuring formula, using the September 2012 RPI inflation rate and a convergence date of 2015/16, indicates that an average rent increase for our tenants of 5.81% from April 2013 will be required, with increases in the following two years of 5.60% and 5.49% based on an assumed inflation rate of 2.5% at September in the relevant years.

The rent restructuring formula is demonstrated below:-

Table 2: Rent restructuring Formula: (50 week rent figures assumed)

Rent restructuring formula	**£**
Average Target (convergence) Rent 2012/13	74.77
RPI at Sept 2012+ 0.5% (2.6% + 0.5% = 3.1%)	2.31
Average Target Rent 2013/14	77.08
Average Actual Rent 2012/13	68.57
RPI at Sept 2012 + 0.5% (2.6% + 0.5% = 3.1%)	2.13
Base Average Actual Rent 2013/14	70.70
Convergence element ((£77.08-70.70)/3)	2.13
Element constrained by limit i.e. RPI + 0.5% + £2	(0.28)
Actual Average Rent 2013/14	72.55

The implications of these changes for our tenants is an average increase in rent of £3.98 per week (5.81%) which ranges from a lowest actual increase of £2.63 (1 bed bungalow) per week up to a maximum of £5.22 per week (7 bed house), with a minimum percentage increase of 4.18% (1 bed house) up to a maximum of 7.87% (bedsit).

In addition to the rent increase outlined above, it is also assumed that Housing Service Charges and Garage Rents are increased in line with the September 2012 inflation level of RPI, i.e. 2.6% where possible and subject to any benefit restrictions. From our review of the Government's Universal Credit Regulations published in December we do not feel there are any significant changes that require the authority to revise its budget proposals.

The increased income from the indicated rent, service charge, and garage rent increases is included in the budget proposals in this report for 2013/14 and the next two years to the convergence deadline. After 2015/16 the Government will effectively assume that the local authorities are on a level playing field with other housing providers, and the rent policy is expected to become one of RPI + 0.5% increases from that point forward.

The authority is notionally free to set a different rent increase. However a number of conflicting assumptions make this very difficult. There is a national rent policy setting out the basis upon which all local authorities and registered providers should set their rents, there are requirements set out within the "Home Standard" set by the Housing Regulator to maintain homes as a minimum to the Decent Homes Standard and the Regulator has also reserved the right to set a "Rent Standard" based upon the application of the national rent policy. Critically for the Business Plan every 1% reduction in rent represents approximately £0.500m in lost rent in 2013/14, and a potential total rent loss over the 30-year business plan of approximately £25m based on assumed future inflation. The Government calculated the debt settlement figures using the increased RPI figures.

Because of the starting level of debt and the low average rents when rent restructuring began, the HRA business plan for the next two years will be very finely balanced. However, in the longer-term over the duration of the 30-year plan, self-financing offers an opportunity to secure the resources necessary to manage, maintain and invest in the existing stock, and potentially invest in new stock.

2.5 Welfare Reform

The Welfare Reform Act received Royal Assent on 8 March 2012 and proposes major changes to the way that welfare support is provided. The Revenue and Benefits Service and North Tyneside Homes have been working on the potential impacts upon both the Authority and our tenants. If all of the reform proposals are eventually implemented there will be significant implications for North Tyneside, as set out below:-

1) Shared Accommodation Rate – around 300 people will lose some of their Housing Benefit (HB) as a result of the extension of this rate;

2) Over 2,000 working age claimants of HB are currently under-occupying their Council tenancy by one or two bedrooms, this would see a reduction of 14% in HB for one bedroom and 25% for two bedrooms under-occupied. It is estimated that this would reduce household income by between £1m - £2m per annum, and have significant risks for the levels of rent arrears;

3) Universal Credit – direct payment to up to 6,000 working age tenants where the HB is currently paid direct to the Authority could impact significantly on arrears, and will be paid 4-weekly in arrears;

4) Localised Council Tax support – There is a potential impact on the level of Council Tax Benefit received by tenants, which could also impact on the level of arrears;

5) There will also be a transfer of responsibility from Department for Work & Pensions (DWP) to local authorities for Community Care Grants and Crisis loans, but with a significant reduction in the resources available;

6) Homelessness – the pressure of the issues identified above could lead to significantly increased pressures on housing advice and homelessness services;

7) Partners – reductions in resources and increased pressure on limited resources will inevitably have a knock-on effect on the partner services of other local support services, such as housing charities and Citizens' Advice Bureau which will see increased pressure for help from their services. Reduced incomes will also have an impact on the local business community; and

8) Workforce – these changes will also place increased pressures on the current workforce as there will be significant administrative changes required to cope with the proposed changes.

Possible mitigations for some of these changes have been included as part of the budget proposals included in this report. Officers across the Council are working to co-ordinate a reasoned authority-wide approach to managing the impact of these changes.

Since the 26 November 2012 Cabinet report was agreed, the Department for Work and Pensions (DWP) has published the re-drafted "Universal Credit Regulations 2013", which will be discussed in Parliament in January 2013, with a view for implementation to start from October 2013. There remain a number of issues to be resolved surrounding these changes, but the re-drafted regulations do give some clarification around benefits relating to service charges. The DWP has now declared that it does not intend to fundamentally change service charge eligibility for benefit. This should be confirmed in the final published regulations, and any final changes will need to be considered for their potential impact on the Business Plan.

In relation to the impact of under-occupancy charges to be implemented from April 2013, and the overall potential impact of Welfare Reform, the Council is still waiting for evidence to emerge in relation to the six pilot authorities who have been implementing the changes already. There is some suggestion that the changes have resulted in significant additional arrears, and discussions with other Local Authorities and Housing Associations has shown a wide range of assumptions being used in Business Plans, anywhere from 1% to 6% of the annual debit, which would range from £0.500m to £3.000m for this authority. It remains unclear what the actual impact on the Business Plan will be, but it is an area that will be monitored very closely. As stated, the proposals included in the 26 November 2012 report and the final Budget proposals include an extra £250k per annum for the next two years into the HRA Business Plan, which will increase the Bad Debt provision to around 1.5% of the annual debit.

Section 3
Cabinet's Final Proposals for the Housing Revenue Account Business Plan and budget for 2013-2015

3.1 Overview

Paragraphs 3.2 to 3.4 below provide the build up of the financial picture for the next two years reflecting:

a) Pressures and Growth
b) The CEI Programme
c) Reserves and Contingency Proposals

3.2 Pressures and Growth

Table 3 below summarises the major pressures and variations faced by the HRA currently built into the budget. These include:-

a) Increase in sums set aside for Debt repayment (Minimum Revenue Provision (MRP);

b) The impact of the change to introduce a true depreciation charge as part of the self-financing changes, utilising the up-rated Major Repairs Allowance (MRA) for up to 5 years;

c) The revenue effects of the proposed Housing Capital Plan;

d) The implications for revenue of the Quality Homes for Older People project – relating to payments to the PFI Contractor and the additional contribution required to be paid by the Council;

e) Increase in HRA Interest charges for refinanced & new HRA debt and changes to Debt Management Expenses & Premiums & Discounts;

f) Increase in House-building Fund contribution – mirrored by increased savings on self-financing debt shown as service efficiency;

g) Increase in the HRA Bad Debt Provision to begin preparations for welfare reform changes from 2013/14;

h) Housing Income Team – additional staff resources due to the pressures brought about by Welfare Reform, which will help with avoiding tenants falling into debt, and helping them to manage their resources where appropriate; and

i) Council Tax Void payments – increase in the provision to cover costs due to changes in the application of void policy – the level of increase will depend on the final option chosen but assumption in Budget proposals is that the first three months void would be free of council tax liability. Currently the first six months void are free of council tax liability.

Table 3: 2013/2014 – 2014/15 Pressures and Growths

Pressures and Growth	2013/14 £000's	2014/15 £000's
a) Debt set aside – MRP	1,400	(3,150)
b) MRA / Depreciation	192	523
c) Capital Plan - Revenue Effects;	(1,727)	5,313
d) Quality Homes for Older People – Contractor and Affordability payments	725	397
e) HRA New Debt / DME / Premiums & Discounts	99	216
f) House-building Fund Contribution	652	0
g) Bad Debt Provision – increase due to Welfare Reform changes	250	250
h) Housing Income Team – additional resources	100	0
i) Council Tax Void payments	200	0
TOTAL Pressures and Growth	**1,891**	**3,549**

3.3 Change, Efficiency and Improvement Programme

As part of the 2013-2015 Financial Planning and Budget process, proposals have been made for additional income, grant and efficiency opportunities. These include:

1. The proposed rent increase brought about by rent restructure changes and rebasing of rent income collectable;

2. Garage and service charge increases;

3. Savings in Debt Interest Charges as a result of preferential loan rates achieved from the Public Works Loan Board for Self-financing loans;

4. Savings in Interest Charges on re-financing of existing Loans via temporary borrowing and long-term re-financing;

5. Savings and efficiencies in relation to management and repairs budgets, including savings in pension deficit funding;

6. Savings from the Quality Homes for Older People scheme re project and procurement costs (including repairs costs due to transfer to PFI Contractor); and,

7. The continued implications of the changes to the Supporting People Transitional Protection.

Table 4: 2013/14 – 2014/15 Change, Efficiency and Improvement Programme

Change, Efficiency and Improvement Programme	2013/14 £000's	2014/15 £000's
1) Income from Rent Increase	(2,719)	(2,802)
2) Garage Rents & Service Charge Income	(63)	(63)
3) Self-Financing – Debt Interest savings	(652)	0
4) HRA Existing Debt – Interest savings from refinancing & temporary borrowing	(424)	(599)
5) Management & Repairs savings (including pension costs)	(377)	(136)
6) Quality Homes for Older People – project & procurement costs	(173)	(200)
7) Supporting People Transitional Protection	(5)	(5)
TOTAL Change, Efficiency and Improvement Programme	**(4,413)**	**(3,805)**

3.4 2013-15 HRA Reserves and Contingencies

The proposed draft budget for 2013/14 includes a contribution to reserves of £0.084m. It is proposed to create a contingency budget of £0.278m to recognise relevant issues including any increases in inflation and any pay award for 2013/14.

Table 5: 2013/14 – 2014/15 Housing Revenue Account Reserves and Contingencies

HRA Revenue Balances	2013/14 £000's	2014/15 £000's
Increase in Contingencies	278	283
Contribution to/(from) balances	84	55
Total Change in Reserves and Contingencies	**362**	**338**

3.5 2013/14 – 2014/15 Draft Housing Revenue Account- Movement on Reserves

Table 6 below summarises the draft Housing Revenue Account movement on balances for 2013/14 – 2014/15, after taking account of the information and details included in Sections 3.2 to 3.4 above:

Table 6: 2013/14 – 2014/15 Housing Revenue Account- Movement on Reserves

HRA Forecast Movement on Reserves	2013/14 £000's	2014/15 £000's
Opening Reserve Balance <u>Add:</u> Change in contributions (to) / from Balances	(1,622) (84)	(1,706) (55)
Closing Reserve Balance	**(1,706)**	**(1,761)**

The budget monitoring position for 2012/13 to 30 November 2012, reported to Cabinet on 14 January 2013, shows projected year-end balances of £1.622m. Hence, a net contribution to balances from the HRA of £0.084m is projected in 2013/14 to give a year-end balance of £1.706m as at 31 March 2014. The budget proposals presented here ensure that a minimum of between £1.000m - £2.000m is retained in HRA revenue balances each financial year covering the two years of the Financial Planning and Budget Setting process, to ensure some measure of contingency and financial stability. These proposals as they currently stand also balance the plan over the longer 30-year period, which is what the Government requires us to demonstrate as part of the self-financing proposals.

3.6 2013/14 – 2014/15 Housing Revenue Account Financial Plan Forecast

Table 7 below summarises the Housing Revenue Account forecast plan for 2013/14 – 2014/15, after taking account of the information and details included in Sections 3.2 to 3.5 above:

Table 7: 2013/14 – 2014/15 Housing Revenue Account Financial Plan

HRA Forecast Expenditure Plan	2013/14 £000's	2014/15 £000's
2012/13 Base Budget <u>Add:</u> Pressures and Growth Change, Efficiency and Improvement Strategy Reserves and Contingencies	0 1,891 (4,413) 2,522	0 3,549 (3,805) 256
Net Forecast Expenditure Variation	**0**	**0**

The rent increases indicated are as required to comply with rent restructuring proposals, and the proposed service charge and garage rent increases. For 2013/14 this increase is 2.6% in line with the September 2012 RPI.

A two-year financial forecast for the Housing Revenue Account is attached at Appendix Band the Housing Capital Plan at Appendix A.

Section 4
Cabinet's Proposals for the 2012-2023 Housing Capital Plan and Prudential Indicators

4.1 Housing Capital Plan 2013-2023

As outlined in Section 2.1 above the final target year for completion of the Decent Homes Programme was 2010/11. The over-riding objective for future years is to ensure that Housing stock is maintained to at least Decent Homes Standard as laid out in the Housing Asset Management Strategy approved by full Council on 9 September 2010. In addition to this if resources allow, there is the added intention of responding to tenant priorities around issues such as fencing and landscaping.

This Capital Plan also provides for the Authority to begin a programme of new build council housing from 2012/13 assuming that enough suitable HRA-owned land can be identified, and planning issues addressed, with the potential for up to 812 new units to be built over the next 30 years in total. This is reflected in the proposed Housing Capital Plan 2013-2023 summarised below and in the attached Appendix A. Some of the main elements of work planned in 2013/14 include:

(a) Kitchens & Bathrooms of £4.573m;

(b) Central Heating and Rewire programme totalling £3.427m;

(c) Disabled adaptations of £1.375m;

(d) Other Targeted Refurbishment Works of £0.715m;

(e) External Works – Fencing / Walling – a new programme to meet one of the major tenant priorities - £1.223m;.

(f) Cyclical / Decoration of £0.693m;

(g) Capital void reinstatements of £1.161m;

(h) Furniture Pack scheme of £0.490m;

(i) Asbestos Works of £0.150m;

(j) Environmental Improvement & Energy Efficiency of £0.455m (including re-programming) and

(k) Re-programming of £0.609m for PFI Homeloss payments;

(l) Other Capital Works – covering ICT Strategy; Water Pipe renewals and Fire Damage reinstatement of £0.316m (including re-programming).

(m) New Build spend on Station Road and Byrness Court - £1.766m.

Table 8 below summarises the 2013-2023 Housing Capital Plan and financing, including potential resources available to fund new builds.

Table 8: Summary of Proposed Housing Capital Expenditure and Financing 2013–2023

Resources	2013/14 £000's	2014/15 £000's	2015/16 £000's	2016/23 £000's	Total £000's
Housing Capital Expenditure	**17,425**	**22,451**	**25,101**	**206,461**	**271,438**
Current Need	**15,187**	**16,286**	**18,333**	**162,930**	**212,736**
Potential New Build	**2,238**	**6,165**	**6,768**	**43,531**	**58,702**
No.of Potential Units	**20**	**45**	**48**	**275**	**388**
HRA Capital Financing					
Major Repairs Reserve/Depreciation	13,012	13,336	13,748	109,705	149,801
Revenue Contributions (HRA)	1,466	6,779	9,328	87,641	105,214
New Homes Bonus	170	0	0	0	170
Capital Receipts (RTB & Other Land Sales)	1,783	1,619	1,308	4,096	8,806
House-building Fund	994	717	717	5,019	7,447
Total Resources	**17,425**	**22,451**	**25,101**	**206,461**	**271,438**

4.2 Draft Prudential Indicators

The Local Government Act 2003 requires Councils to comply with the 'CIPFA Prudential Code for Capital Finance in Local Authorities.' The Prudential Code requires authorities to develop a set of Prudential Indicators for capital as laid out in the Code. In addition to the indicators laid down in the Code, local authorities are free to set up their own local indicators, as they consider appropriate.

The following part of the report sets down the draft Prudential Indicators as calculated and proposed for the Housing Revenue Account for North Tyneside Council for 2013–2015.

4.3 Indicators of Affordability

Prudential Indicators (PIs) 1 to 4 are key indicators of affordability.

4.4 Ratio of Financing Costs to Net Revenue Stream (PIs 1 and 2)

This indicator shows the estimate of the ratio of financing costs to net revenue stream for the current and future years, that is the proportion of the budget for Housing that is spent on the financing of capital spend. The estimates of financing costs include the base Capital Plan, and the implications of the additional debt taken on from 2012-13 in relation to the self-financing settlement. It also includes the estimated financing costs of the Quality Homes for Older People PFI Project.

The actual figures for 2011/12 are also set out in Table 9 below:

Table 9: Ratio of Financing Costs to Net Revenue Stream (PIs 1 and 2)

	2011/12	2012/13	2013/14	2014/15	2015/16
	Actual	Est.	Est.	Est.	Est.
HRA	17.14%	27.63%	31.11%	28.47%	30.74%

The above indicator shows costs for all borrowing, both supported and unsupported. To enhance the information available for decision-making we have also provided a local indicator to show the proportion of the budget that is spent on unsupported borrowing. This is shown in Table 10 below:

Table 10: Ratio of Financing Costs for prudential (unsupported) borrowing to Net Revenue Stream (PIs 1 and 2)

	2011/12	2012/13	2013/14	2014/15	2015/16
	Actual	Est.	Est.	Est.	Est.
HRA	4.04%	8.18%	10.20%	4.47%	4.96%

4.5 Impact on Council Tax and Housing Rents (PIs 3 and 4)

This prudential indicator reflects the estimate of the incremental impact of capital investment decisions proposed in this budget report, over and above capital investment decisions that have previously been taken. These figures reflect the amount of capital funded by the HRA arising from the proposed Capital Plan.

Table 11: Impact on Council Tax and Housing Rents (PIs 3 and 4)

	2013/14 £	2014/15 £	2015/16 £
For average weekly housing rents	-2.67	7.09	3.73

4.6 Capital Expenditure (PIs 6 and 7)

The actual capital expenditure that was incurred in 2011/12 and the estimates of capital expenditure to be incurred for the current and future years are set out in Table 12 below:

Table 12: Capital Expenditure (PIs 6 and 7)

	2011/12 Actual £000's	2012/13 Est. £000's	2013/14 Est. £000's	2014/15 Est. £000's	2015/16 Est. £000's
HRA Total	**13,660**	**19,632**	**17,425**	**22,451**	**25,101**

These estimates mirror those shown in Table 8 of this report.

4.7 HRA Capital Financing Requirement (CFR) (PIs 8 and 9) and CFR Debt Limit

The Capital Financing Requirement measures the authority's underlying need to borrow for a capital purpose. It reflects the cumulative amount of borrowing required for capital purposes less the annual Minimum Revenue Provision (MRP). In accordance with best professional practice North Tyneside Council does not associate borrowing with particular items or types of expenditure.

Under the self-financing regime introduced by powers enacted under the Localism Act 2011, the Authority is limited to a maximum HRA CFR. This means the cumulative HRA borrowing must not exceed this limit on the 31 March of the relevant financial years. These figures assume that the CFR limit will be flexed by Government, to allow for the implications of the Quality Homes for Older People PFI scheme:

Table 13: HRA CFR Limit

	2012/13 Est. £000's	2013/14 Est. £000's	2014/15 Est. £000's	2015/16 Est. £000's
HRA Total	**292,465**	**317,066**	**350,217**	**366,198**

The actual CFR is reduced by any MRP that is set aside by the Authority. As at 31 March 2012, the HRA CFR (excluding PFI and leases) was £290.824m.

Estimates of the end of year Capital Financing Requirement for the HRA for the current and future years and the actual Capital Financing Requirement at 31 March 2013 are set out in Table 14 below:

Table 14: Capital Financing Requirement (PIs 8 and 9)

	2011/12 Actual £000's	2012/13 Est. £000's	2013/14 Est. £000's	2014/15 Est. £000's	2015/16 Est. £000's
HRA	290,824	288,324	309,025	340,457	352,664

These figures include estimated implications of the Quality Homes for Older People PFI.

The above indicator shows the total borrowing requirement, both supported and unsupported. To enhance the information available for decision-making we have provided a local indicator to show the Capital Financing Requirement for unsupported borrowing. This is shown in Table 15 below:

Table 15: Capital Financing Requirement for Unsupported Borrowing (PIs 8 and 9)

	2011/12 Actual £000's	2012/13 Est. £000's	2013/14 Est. £000's	2014/15 Est. £000's	2015/16 Est. £000's
HRA Total	47,406	44,906	41,006	40,256	38,756

Cabinet should note that these Prudential Indicators are specific to the Housing Revenue Account (HRA). However, the full Prudential Indicators for the Authority as a whole will be agreed by full Council as part of the 2013-2015 Financial Planning and Budget Setting process.

Section 5
Response to the Overview and Scrutiny recommendations

5.1 Information Document

This section of the document sets out the process for Cabinet to respond to any recommendations made by the Overview and Scrutiny Committee following their meeting on the 7 January 2013.

The Cabinet must formally respond to any recommendations made by the Overview and Scrutiny Committee in considering its final budget proposals. It is therefore proposed that Cabinet consider any recommendations at this meeting of 16 January 2013 prior to approving this report.

A supplementary paper to this report will be issued ahead of the Cabinet meeting on 16 January 2013 containing Cabinet’s response to any Overview and Scrutiny Recommendations that may arise.

Section 6
Housing Revenue Account-Statement to Cabinet by Chief Finance Officer

6.0 The Local Government Act 2003 imposes duties on local authorities in relation to budget setting. The Act requires that when an authority is deciding its annual budget Members and officers must take into account a report from the chief finance officer on the robustness of the budget and the adequacy of the authority's financial reserves.

Government has a back up power to impose a minimum level of reserves on any authority that it considers is making inadequate provisions.

In making the statement the chief finance officer necessarily places reliance on information provided to her by other officers of the Authority as part of the budget setting process. Due cognisance to CIPFA's guidance in relation to the adequacy of reserves and balances will also be taken into account.

This statement is made specifically in reference to the Housing Revenue Account. As this meeting of Cabinet is receiving and approving the HRA budget and business plan, it is considered appropriate to include a statement to Cabinet by the chief finance officer in this report.

6.1 Housing Revenue Account Statement

Robustness of Estimates

In assessing the robustness of estimates, the Chief Finance Officer has considered the following issues:

- The general financial standing of the HRA;
- The underlying budget assumptions from the HRA financial strategy;
- Future budget pressures and growth proposals, ;
- The adequacy of the budget monitoring and financial reporting arrangements in place;
- The adequacy of the Council's internal control systems, relying on the Assurance Statements provided as part of the Annual Governance Statement for the 2011/12 Annual Financial Report , presented to Council on 27 September 2012;
- The adequacy of unearmarked and earmarked reserves to cover any potential financial risks faced by the HRA; and,

- The implications of Government's 2011 – 2015 Spending Review and the Local Government Finance Settlement on the HRA Business Plan.

The chief finance officer is satisfied that due attention has been given to the 2013-2015 Housing Revenue Account and associated business plan.

The Cabinet is aware it must keep under review its 30 year Housing Revenue Account Business Plan in the context of its Financial Planning and Budget Setting process and the Sustainable Community Strategy and known key financial risks. Future pressures need to be considered and the Authority should not take 2013/14 in isolation to future years' needs and pressures. Each year's Housing Revenue Account budget must continue to be considered within the context of the 30 year Business Plan, the ten-year Housing Capital Plan and delivery of the Sustainable Community Strategy.

To ensure that the HRA continues to keep within its approved budget and the financial integrity of the HRA is maintained, it is essential that budget holder responsibility and accountability continues to be recognised as set down in the Authority's Financial Regulations and in the roles and responsibilities section of the Authority's budget management handbook.

6.2 Adequacy of Financial Reserves

The HRA budget proposals for 2013/14 assume that there will be no drawdown of reserves used to support the 2013/14 HRA budget, instead there will be a £0.084m contribution to reserves, with an average assumed rent increase based on the Government's rent restructuring formula of 5.81%.

The chief finance officer's view is that these decisions are required in order to manage and meet the identified needs of the HRA Business Plan for 2013/14, and to place the HRA in a position to begin to meet the aspirations for a self-financing HRA over the next 30 years. HRA Balances are budgeted to be £1.706m at the end of 2013/14 which is an increase from an estimated figure of £1.622m at the end of 2012/13. In accordance with the Reserves and Balances Policy, the adequacy of this reserve has been reviewed and it is the chief finance officer's view that the HRA reserve balance should be maintained between £1m to £2m over the life of the Business Plan as a minimum. Any decision to implement a different policy decision in relation to the rent increase and use of reserves will have a potentially damaging impact on the future HRA unless significant compensating savings can be identified.

Guidance on Local Authority Reserves and Balances is given in Accounting Bulletin LAAP (Local Authority Accounting Practice) 77. This states that *"Balancing the annual budget by drawing on general reserves may be viewed as a legitimate short term option",* and so the proposed HRA 2013/14 budget does not contradict the issued guidance. The Bulletin does then go on to say *that "It is not normally prudent for reserves to be deployed to finance current expenditure"*. The 2013-2015 HRA budget and associated business plan have been developed so that ongoing revenue expenditure is aligned to annual income with no long term reliance on reserves.