Agenda Item 9

Housing Management
Salisbury District Council, 26 Endless Street
Salisbury, Wiltshire SP1 1DR

direct line: 01722 434351
***fax*:** 01722 434530
***email*:** dstreek@salisbury.gov.uk
web: www.salisbury.gov.uk

Report

Subject : Housing Local Authority Special Purpose Vehicle

Report to : The Cabinet

Date : Wednesday 18 June 2008

Author : Head of Housing Management

Cabinet Member for Housing : Councillor Ian Tomes

---

1. **Report Summary:**

The Housing Quality Network (HQN) have been asked to provide a paper examining the potential to provide more council housing to assist with the priority of providing more affordable homes and supplement the development currently being undertaken by our Registered Social Landlord partners. This report is designed primarily as a discussion document to consider new build by the local authority before considering setting up a special purpose vehicle to bring forward individual schemes.

2. **Background**

2.1. The Housing and Regeneration Bill, now past its second reading in Parliament, will provide local authorities with the potential to provide more council owned properties. As part of the work in developing the new 30 year Housing Revenue Account Business Plan it became apparent that there could be some advantages from this emerging legislation to both the existing stock and for the delivery of new affordable housing as part of an overall strategy for the management of our assets .

2.2. HQN, who are working with us on the development of the Business Plan, were therefore asked to provide a paper, in the wider context, of the opportunities this affords us in our current situation. The report is attached as ***Appendix 1***.

3. **Report Findings:**

3.1 The report provides details of the development of the current governments thinking and powers it has or is about to provide for local authorities to assist with it's affordable housing agenda. In particular the government has acknowledged that land held by local authorities needs to be released to enable sufficient development and has set out a range of options to increase the flexibility with which authorities might bring it forward which whilst continuing to see traditional RSL/developer schemes as the mainstream delivery mechanism, provides the scope for a new type of council house building to make a significant contribution.

3.2 It concludes that the council should be able to take advantage of the favourable policy environment for new build housing in the forthcoming period. Furthermore it suggests that a special purpose vehicle could be established almost immediately and providing suitable sites and schemes can be found, initial modelling and development appraisal work undertaken.

4. **Other factors**

4.1 Clearly this issue cannot be treated in isolation from the move to one council. In fact it provides even more opportunities with the potential for more public authority land being available both within South Wiltshire and beyond and could assist with the LAA affordable housing targets. If members are minded to pursue this then authorisation will need to be sought from the Implementation Executive**.**

5. **Consultation Undertaken:**

5.1 A copy of the report from HQN has previously been provided to the Portfolio holder. The tenants panel are due to consider this report at their next meeting on the 23rd June 2008.

6. **Recommendations:**

6.1 To discuss whether members wish to pursue this opportunity further. If so;

6.2 To recommend to the Implementation Executive that further work should take place to look at establishing a special purpose vehicle and that HQN be retained for that purpose

7. **Background Papers:** Draft Initial Report from HQN

8. **Implications:**

- **Financial:** None at this stage. The attached report highlights potential major financial implications in the future, these would have to be considered more fully if the Council/ I.E. was minded to develop the business case further.
- **Legal** :
- **Human Rights** : None.
- **Personnel** : None.
- **Climate Change** : None.
- **Council's Core Values** : Excellent services.
- **Wards Affected** : All.

Appendix 1

SALISBURY DISTRICT COUNCIL
OPTIONS FOR NEW AFFORDABLE HOUSING IN SALISBURY
Initial Draft Report April 2008

Contents

1 Introduction

1.1 Background

Following a stock transfer 'no vote' in 2006, Salisbury District Council is now developing its plans for the future maintenance of its housing stock, the development of the housing service and for the provision of new and replacement affordable housing. Given pressures within the business plan, the council is keen to understand the potential:

- To use existing assets such as housing, other buildings and land in a more proactive way to better meet housing needs,
- For building new local authority housing in a new housing company and
- For the alternatives for the financing of the HRA stock to emerge in the forthcoming period including Housing Revenue Account self-financing.

Drawing upon our work with the council on the development of the Housing Revenue Account business plan and on the national self-financing pilot project, HQN have been invited to provide an initial briefing report on the progress nationally towards innovation in new build from local authorities. At the same time, we have also provided an up to date commentary on the national progress towards self-financing and subsidy reform, particularly given that both the new build and self financing initiatives are driven by clauses within the Housing and Regeneration Bill, now past its second reading in Parliament. The Bill itself draws heavily upon the Housing Green Paper, which was published in July 2007.

The direction of travel within the national agenda for new build and for the relaxation of financial constraints as set out in the Green Paper is more favourable towards expanding the role of local authorities than perhaps for a generation and Salisbury DC needs to consider the future in the context of the likelihood that the existing stock will remain in the ownership of the council well into the next decade.

This direction of travel is more than adequately exemplified by the announcement of a fundamental 'root and branch' review of the HRA subsidy system by the Housing Minister, in which all aspects of council housing finance are being reviewed and which began on 10 March. A progress report on the review is set out below.

The experience of a 'no vote' can often set back council housing services several years, both in terms of the challenges offered in meeting the investment needs of the stock and in improving service delivery - and also in terms of morale and the appetite for taking a positive view about the future. Our work with the council on the HRA business plan indicated that there will be insufficient resources to maintain existing stock beyond anything other than the very short to medium term and that there are long term challenges in making the business plan more viable. One key area of enquiry therefore might be consideration of the future of existing stock in the context of opportunities for redevelopment to promote greater sustainability in the future.

Together with other significant policy initiatives (discussed below), the council may be able to take advantage of this policy future and develop solutions for both the existing stock and for the delivery of new affordable housing as part of an overall strategy for the managing of its assets, therefore delivering a stock investment strategy that is potentially more sustainable and more financially viable.

1.2 Background

The Government is very keen to support innovation in new development schemes, be that in design or in the financial models for delivery. Pilot projects have been established with other authorities. The council wishes to examine the potential for new build in the Salisbury context given this progress. This paper follows the ongoing process to finalise the HRA business plan and an initial briefing from the Head of Housing in early 2008 and sets out for discussion the following:

1. A summarised commentary on national progress for new build local authority housing,
2. A discussion of the self financing project and the extent to which this could be applied in the Salisbury context, together with the possible implications of the subsidy review.
3. Outline suggested areas to further develop thinking and feasibility.

A key objective for all councils within such a review is to understand the legal and financial boundaries in the context of Government policy. Whilst the policy signs are positive, there remain certain barriers to the delivery of some ideas and a clear awareness of these is critical to inform future thinking.

This initial draft report is intended to act primarily as a discussion document and we have not as yet undertaken any specific modelling or analysis to support any suggested possible schemes. It is true to say that all councils considering new build begin with such a high level discussion before beginning to think about bringing forward individual schemes for consideration.

2 The Green Paper and national policy progress

2.1 Green Paper: a quick tour

The Housing Green Paper: *Homes for the Future: more affordable, more sustainable* was published in July 2007 and subsequently many of the measures outlined appear in the Housing and Regeneration Bill published in November of that year. The paper contains a wide ranging discussion of the need for additional affordable housing and sets ambitious objectives for increased delivery and increased funding. Problems with affordability are now more or less universal across England and all local authority areas have large unmet housing needs and demands. The objective is for 3 million more homes by 2020 with annual completions rising to 1960's levels of 240,000 per year, with at least half of these affordable. New housing will be built to higher densities generally and all will be carbon neutral by 2016.

The Green Paper set out a series of initiatives which, while setting objectives to increase the amount of housing delivered through the existing mainstream methods (ie Housing Association/Developer schemes), also set out the need to bring forward land and assets held by public bodies (particularly local authorities) to enable new build, land and assets that might not usually come forward in those type of 'traditional' schemes.

There are initiatives to assist (through incentives and intervention) the delivery of housing strategic objectives including:

- A greater role for the new Homes and Communities Agency to direct development within housing strategies
- A requirement on authorities to identify land for development at least 5 years ahead
- The bringing forward of public sector land for development (land for some 200,000 homes)
- Increases in Planning Delivery Grant for those authorities successful in bringing forward sites for delivery.

The key to the delivery of a quantum leap in new housing is the availability of land and the Government has acknowledged that land held by local authorities is needed to enable the development necessary. In order to release land for development, the Green Paper therefore set out a range of options to increase the flexibility with which authorities might bring it forward, a series of options which, whilst continuing to see traditional RSL/developer schemes as the mainstream delivery mechanism, do set out the scope for a new type of council house building to make a significant contribution.

Most of the ideas in the Green Paper have subsequently been included in the Housing and Regeneration Bill including a commitment to reform of the HRA subsidy system to allow authorities to leave the subsidy system and become self financing, retaining their rents and income locally.

2.2 Setting the scene: before the Green Paper

In fact, the progress of policy towards enabling local authority new build has been developing for a while. The key milestones have been:

- The Local Government Act 2003 which introduced the Prudential Code, allowing local authorities to borrow prudentially without government permission, providing the borrowing is affordable; this Act also abolished Local Authority Social Housing Grant through which councils could provide resources to RSLs for new build and reclaimed grant via the Housing Corporation.

- The Local Government Act 2000, which established the power to act in the general 'Well Being' of the local community in delivering policy and services.

In addition, the Local Government and Housing Act 1989 has provided the power to set up local authority companies to further the aims of the authority since 1990.

At the same time, the emergence of Arms Length Management Organisations (ALMOs) as a dynamic and high performing sector since 2002 around the delivery of the decent homes standard has acted as a spur to develop thinking in terms of broader local government involvement in wider aspects of housing delivery. The Government's Review of the Long Term Viability of ALMOs, which reported in June 2006, offered the potential for an expanded and more flexible role in future delivery, including:

- Setting the scene to allow ALMOs to bid for Social Housing Grant from the Housing Corporation by becoming preferred partners along with Housing Associations and private developers
- Inviting six case study local authorities (three with ALMOs) to participate in further developing thinking towards freedoms and flexibilities for the HRA (reference below).

2.3 New models of supply and removing financial constraints

In summary therefore, the Green Paper and the Bill effectively draw all of these policy strands together in encouraging council housing new build on local authority housing land which might not otherwise come forward for development or redevelopment. The key headlines are:

- 14 local authority local housing company pilots to work in partnership to develop new housing owned by a subsidiary or 'Special Venture Vehicle' company,
- 10 Community Land Trust pilots for developing land in rural areas for joint 'home ownership' in community owned trusts,
- The introduction of powers to release authorities from the HRA subsidy system with agreements which would cover some or all of their properties,
- The removal of existing financial constraints for new build properties in the HRA.

The ability for non-registered social landlords (developers and other bodies) to apply for Housing Corporation grant has also developed significantly. Eight ALMOs and two local authorities (with subsidiary companies) became pre-qualified for development partner status with the Housing Corporation in 2007 and four of these subsequently became the first local authority bodies to receive grant. An intermediate bidding round for applications is in progress during 2008.

The current financial constraints on HRA new build are twofold: 1) that some of the rent income from a new property is lost in negative subsidy and 2) that HRA properties are subject to the Right to Buy and future sale would mean 75% of the proceeds pooled by the Government. New build through an ALMO or LA housing company is outside the HRA and therefore not subject to these constraints although 100% ownership by the authority does mean that any borrowing undertaken would count as 'public expenditure'. An additional attraction of development through subsidiaries is the retention of the asset on the council's 'ultimate' balance sheet.

2.4 Housing and Regeneration Bill

Legislation to relax constraints on new local authority build is included in the Housing and Regeneration Bill (originally clause 269):

- Allow new build in housing companies outside the HRA,
- Allow HRA new build after a set date to be outside of the need to pool rents of RTB receipts,
- Develop a self financing approach for some authorities for their existing stock.

As the bill was published, many authorities and ALMOs had already been exploring the opportunities for development through subsidiaries and a short note of progress is set out below. At the time of writing, the Bill has passed second reading and is currently in committee stages within Parliament. All the indications are that the relevant clauses pertaining to the relaxation of constraints will become law as none have been the subject of any amendments to date. In fact the clause has received cross party support.

2.5 Experiences nationwide

Across the country, there is a great deal of discussion and activity about developing ideas for the building new Local Authority and ALMO-owned housing. Most ALMOs (with their authorities) and a significant number of local authorities with retained management are exploring the opportunities.

Perhaps given progress on decent homes, early ALMOs have made the most progress although some authorities have also been at the forefront. The following are examples of the type of schemes that are being developed. Generally, developers are very interested in working with LAs and ALMOs on these types of schemes so there have been no difficulties in finding potential partners.

CityWest Homes have reviewed the entire portfolio of sites in Westminster's HRA and have arrived at around 20 development opportunities. Most of these would involve redeveloping existing flatted estates to increase the density of housing. In some cases, some vacant plots (for example in-fill using sites which are currently poorly maintained garages) have been identified where some new build could take place without clearance.

Your Homes Newcastle, a 2 star ALMO, gained council approval in April 2007 to invite tenders to develop around 30 bungalows on in-fill sites around the city on a no grant, no borrowing basis. This is the first phase of an ambitious programme to provide nearly 1,000 new bungalows on a range of small sites across the city. The scheme is founded upon the free transfer of HRA land to the ALMO and of the total development of 30 units, a number will be sold on the open market and perhaps some on a shared ownership basis with the remainder for rent at either social or intermediate rent.

Hounslow Homes has proposed the building of a new 30-unit development of flats on a cleared site where all of the building costs will be paid for by sales proceeds. There would therefore be no need for grant funding and no need for borrowing. The ALMO is partnering with a developer who would take the risk on the development and put up the initial finance. Hounslow Homes have also been successful in gaining £17m grant from the London Housing Board to help redevelop three sites where there are currently non-traditionally built flats, increasing the amount and quality of affordable housing. Land use would increase from less than 100 poor properties to over 400 new with over half for affordable rent.

Other ALMOs actively looking at schemes include Derby City Council with Derby Homes with a significant programme for redevelopment of 1930's low density housing estates, Kirklees Neighbourhood Housing, Bolton at Home and the Brent Housing Partnership, all of which have become eligible to bid for Social Housing Grant.

Leading the way for authorities have been Runnymede, Woking and Barking and Dagenham, each with 100% owned subsidiaries for new build and acquisition. Leicester City Council has a model of a minority owned company enabling borrowing outside of public expenditure constraints, involving the sale of defective LA stock to the company and the recycling of sales proceeds as grant to the company to enable refurbishment.

Derby Homes, Sheffield Homes and Brent Housing Partnership together with Knowsley MBC have been allocated grant for their schemes in 2008 and are the first local authority bodies to receive such grant for nearly 30 years. A further three ALMOs will receive grant passported via partner Housing Associations (including Stockport Homes, Solihull Community Housing, Wigan and Leigh Homes).

It is worth noting the common features of these schemes:

- The bringing together of strategies for dealing with current stock and available land and the opportunity to build or replace with new housing,
- The need for partnership with a developer/contractor (which could be an RSL),
- The aim to reduce the reliance on grant and borrowing in the early days in order to build up experience and a track record,
- The relatively small scale of initial schemes to develop experience,

- The better use existing council (HRA) owned land to increase densities and to mix the tenure and property design of communities.

3 Factors affecting LA new build and company models

This section represents a short summary discussion of the key financial issues and considerations. When actively considering the establishment of new companies, the council would need to engage specialist legal advice and the short commentary below is included for completeness only as we are not qualified to give a formal legal opinion.

3.1 Financial considerations for new build

Social and affordable housing is unable to be funded by borrowing alone without some form of subsidy from another source, be that up front resources to reduce the reliance on borrowing or the cross subsidisation of borrowing charges from the rents of other properties. The options for raising resources to provide the ‘up front’-injection necessary to ensure long-term affordability of new developments are set out below.

The various routes to the funding of new housing are generally through three sources:

- Borrowing – repaid from future net rental income
- Grant - or other form of up front resource
- Cross-subsidisation from sales – where some properties are built for sale of shared ownership and the net sales proceeds are utilised to fund the ‘grant’ requirement for rented properties.

The pattern of a traditional RSL scheme is for funding to come from Housing Corporation (or local authority) grant and borrowing. Mixed tenure schemes (eg through Section 106 requirements) are increasing in range in line with the move to mixed communities and utilised to cross-subside from sales proceeds and to keep grant rates down. This delivers more affordable rented housing for the same grant resource and mixed tenure communities.

The relative absence of track record of development for local authorities and ALMOs, means that Homes and Community Agency grant might be less important in the funding of schemes in the short term and a mix of borrowing and sales proceeds are the predominant funding sources. Local companies are however eligible to bid (as set out above).

Possible sources of ‘local funding’ include:

- Useable, non-pooled, Right to Buy receipts
- Other receipts from the disposal of housing assets (non Right to Buy) where 100% of proceeds can be recycled towards affordable housing
- Commuted Section 106 sums from off site contributions from developers

- Housing Corporation Grant: available to ALMOs and local housing companies to pre-qualify then bid for, using the financial status of the parent council.

Some of these might be available in the Salisbury context.

3.2 Technical and other considerations

A schedule of key issues, drawn from experiences of the development of new housing companies around the country is set out below.

3.2.1 Tenancy type

Rented properties held by a local company are outside of the HRA and therefore able to be let on Assured Tenancies, similar to those operating for Housing Associations.

Some aspects of the HRA secure tenancy can be developed for a new type of tenancy within the company. This can include such issues as the Right to Buy where the financial constraints operating for the HRA are removed.

3.2.2 Rent levels

The scope to let tenancies on an assured basis gives the opportunity, subject to local policies and preferences, to vary rents away from the 'social rent' level implied by rent restructuring.

Whilst most LA/ALMO new build is at the social rent level, some organisations are exploring the possibility of intermediate rents, above social rents but still below market rent levels for certain client groups.

The benefits are mainly financial in that rent increases above social rents have a disproportionately high 'gearing' in reducing the reliance on grant funding. An increase in rents of 10% might reduce the need for grant/subsidy by up to 20%.

Conversely, the implementation of such an approach needs to be managed appropriately in terms of which properties and which client groups are focused upon.

The purchase of properties on the open market would necessitate higher rents to lever in greater borrowing.

3.2.3 Borrowing

All borrowing by a subsidiary which is more than 50% owned by the council scores as 'public expenditure' and therefore falls within the rules governing LA Prudential Borrowing. Generally, the scope to take out borrowing is dependent upon the ability to cover the debt and eventually repay it (if appropriate) which for housing to be let to applicants on a long waiting list would not present any issues. The council's prudential indicators would be updated accordingly.

However, there are two issues which arise from borrowing undertaken by a company which affect the potential financial viability of schemes:

- The borrowing would almost certainly come under the consolidated interest rate applying to all authority debt and be charged to the company at this rate irrespective of the actual loan rates obtainable. CIPFA have recently been asked to re-confirm that this is the case. This may be positive or adverse to the company depending upon current loan and average interest rates although the pooling of loans should act to smooth interest rate changes felt by the company.

- The borrowing is outside of the HRA and, under previous regulations, would have been subject to a 'Minimum Revenue Provision' set aside of 4% pa. CLG have however changed the Capital Financing Regulations and have adopted an approach to allowing set aside to be on the basis of asset life, many are arguing for a minimum 60 year life (implying set aside of 1.67%) or 80% (set aside £1.25%) for housing built in subsidiary companies – this is a matter for the Chief Financial Officer of the council.

A third issue is the actual mechanics of the borrowing – the most common proposal at this stage is for the council to carry out the borrowing and 'on lend' to the company, perhaps with a premium, subject to the fundability of the scheme overall and the subject of a specific 'loan agreement' between the council and the company.

3.2.4 Management and maintenance

A key advantage of building or redeveloping/transferring homes to a LA housing company is that consistency of management is maintained. Both the Government and Audit Commission are known to be critical of the dispersal of RSL housing arising from piecemeal land and stock transfers.

The new company route can take advantage by ensuring that current landlord services within the council can continue to provide management and maintenance services, paid for under contract from the rent. Loss of stock through the HRA and replaced in the company might not therefore have the impact in terms of reduced management cost needs into the future and the economies of scale of a large stock base maintained.

Several schemes are already established whereby local authority housing services provide management services to other landlords and housing providers and this is a key way to enhance the sustainability of the HRA business plan whilst addressing major issues of investment.

3.2.5 VAT and tax issues

The establishment of a new housing company for development and ownership of housing might have implications for the realisation of surpluses and payment of VAT and Corporation Tax.

Formal and separate legal advice should be engaged at an appropriate time but we understand from developments at other authorities that a direct LA subsidiary can continue to benefit from the VAT advantages of the authority providing an appropriate legal form is adopted.

There are options around the adoption of charitable status which has tax benefits but which might restrict future operational flexibility. Charitable status removes tax on profits but limits the use of those profits to the aims of the company.

Taxation is also likely to apply to land transfer, even if this is at nil value. Stamp Duty Land Tax would be payable on notional values even in the circumstances of transfer to a 100% owned subsidiary unless the company was charitable.

Many of these issues are being discussed and debated nationally and remain to be resolved formally although it is known that the government wishes to remove these barriers where they are found. At this stage, any financial modelling created to support development or company scheme appraisals should therefore ensure that VAT and tax payable are at least incorporated as sensitivities to the modelling.

4 HRA Self financing

4.1 Introduction

In recent years, the financing of council housing has come under increasing pressure. Despite large investment in stock to meet the Decent Homes Standard, the resources made available to local authorities through the HRA revenue subsidy system have continued to decline in real terms. The impact of rent restructuring and targeted convergence with the RSL sector has led to rent increases well above inflation for most tenants. This has been coupled with the increasing control of expenditure through allowing inflation-only increases in expenditure allowances. Salisbury's overall negative subsidy has risen sharply to over £7m in 2008/09.

Since July 2006, CLG have been piloting the idea of 'self financing' – leaving the subsidy system with a one off adjustment to the HRA's finances – with six authorities. The final report from this project was published on 10 March. This section summarises the possibilities for self financing.

As a result of some of the findings within the project, the Housing Minister announced in late 2007 a 'root and branch' review of the subsidy system to commence immediately.

4.2 The future of subsidy and the Subsidy Review

The subsidy system has come under pressure in reports from national bodies such as the Audit Commission and Chartered Institute of Housing which highlight that:

- The system is increasingly complex and the inter-dependencies of all authorities make for increasing volatility in settlements.
- The unpredictability does not allow sensible long term planning.
- The system is under-funded and the situation is getting worse: if current policies are unchanged, the system will go into very large 'overall surplus' as rents pooled by the Government will rise faster than expenditure allowances and these rental surpluses are captured at the national level.
- There is a strong case for reinvesting future rental surpluses in council housing given current and likely future conditions.

The Government has admitted that the system is moving into overall surplus announcing in Parliament on 18 December 2007 that the likely overall surplus in 2008/09 is £190m rising to over £300m by 2010/11.

The Government appears committed to finding a more sensible long term solution and the announcement of a fundamental review is therefore a positive move.

The review is addressing the following four areas:

- The costs and standards of running and maintaining/improving council housing
- Rents and service charges
- The mechanism of resource distribution – whether there continues to be a national subsidy system and how self financing might develop
- How the HRA operates locally.

A fifth work stream will take an overall view of progress and a final report is expected in the spring of 2009. A series of workshops with expert advisers have been convened to support the work stream inquiries and the initial round of meetings is taking place in April and May. Further research is expected to be commissioned and considered as a result of the need for evidence to support the review. Further meetings will take place in the summer and autumn of 2008.

The review is being overseen by a Programme Board comprising CLG and Treasury representatives. The main outcomes are expected to address both the medium term issues arising from the next Spending Review period and a longer term view of the sustainability of council housing in England.

The review could represent a real opportunity to make a fundamental change to the future financing of council housing. Of more immediate concern will be the impact on future likely subsidy settlements and resource allocations in the period from 2010 onwards.

The review is unlikely to lead to a worsening of the financial position nationally (and therefore for Salisbury) - the *extent* to which the position improves in the medium to long term and whether the government will be prepared to allow financial freedoms locally are the key issues at stake.

4.3 Fundamentals of self financing

The principles of self financing lie in the original 'Blue Skies' paper of August 2002: '*The Way Forward for Housing Capital Finance*'. In this paper, the idea was first mooted of high performing authorities coming out of the subsidy system following a one off adjustment to the HRA's finances, and no longer paying over or receiving subsidy. The issue was subsequently taken up by the National Federation of ALMOs as part of the long term review of ALMO viability which began in September 2004 and reported in June 2006. The outcome was the pilot project which began in September 2006 and is concluding shortly.

The one off adjustment would take place on the basis of a commutation of all future subsidy flows into a single payment to or from government based on the Net Present Value (NPV) of 30 years of subsidy. For authorities likely to be in negative subsidy into the longer term, this would involve borrowing to 'buy out' of the system; for authorities likely to remain in subsidy over the longer term, this would involve a reduction in housing debt to ensure long term viability.

As the policy agenda with regard to the future of HRA subsidy and the self financing pilot project is developing so rapidly, the precise implications for self financing are as yet unclear but what is clear is that:

- The Housing and Regeneration Bill contains a clause (previously 269) to give ministers the power to take HRA properties (new and existing) outside of the subsidy system.
- There is a commitment to the six pilot authorities that implications of work carried out on the viability of self-financing will be taken forward.

The criteria for pilot status included Excellent CPA with a Good Housing CPA score and it could be expected that qualification criteria would apply in the future. Salisbury DC would need to have a firm plan to achieve first 2 then 3 stars within housing services and the equivalent of a minimum good CPA corporately as a likely pre-requisite to accessing any freedoms and flexibilities which might become available in the short to medium term.

CLG thinking is focused on the first live pilots by April 2010. In addition, there may be opportunities for authorities such as Salisbury to engage proactively in the review and to further test the viability of self financing locally. Salisbury shares the characteristics of many authorities where a proposed transfer has received a no vote in that there is no access to additional central funding for decent homes, and the pressures within the business plan are greater than for other retention authorities. Thought might be given to how the council might actively engage in the review process particularly given the absence of a long term viable plan for investment in and maintenance of the existing stock.

4.4 What might self-financing deliver for authorities like Salisbury?

The pilot project has highlighted the key benefits from self-financing:

- The efficiencies of long term planning without the unpredictability of the subsidy system, estimated at around 10% by the pilot authorities.
- Future rental surpluses would be available locally rather than pooled nationally, with more headroom to borrow to improve stock and neighbourhoods to a higher standard than possible under current rules.
- The ability to develop housing and redevelop/remodel housing without the need to lose land and assets as a result.

In the Salisbury context, this could mean some or all of the following:

- An increased investment standard adopted with and for tenants with increased viability for the existing stock,
- Stability in the business plan would lead to a much firmer footing for service delivery over the long term, with the potential for investment in service delivery after the decent homes standard is achieved,
- The ability to fund HRA investment from internal HRA resources (borrowing and revenue) allowing the potential reallocation of RTB and other capital receipts to General Fund programmes, receipts which could be put to towards meeting the need for new affordable housing, including through a new company,
- The ability to deliver new build via the HRA or via the establishment of a council-owned local housing company where the critical mass of the existing stock can be used as additional leverage for capital finance and borrowing.

Against these, increased risks apply to interest rate management and having local responsibility only for the maintenance of stock.

4.5 Key findings nationally

What could be delivered in the short to medium term depends very much on the financial basis for the one-off settlement. The critical factor is the assumption about future subsidy behaviour which forms the basis of the ‘settlement’. The Government has initially adopted a ‘no change’ position ie that rents will continue to increase by inflation plus 0.5% after converging with targets whilst expenditure allowances will increase by inflation only. The increased future rental surpluses over the longer term lead to very high levels of ‘buy out’ settlement.

As the same time, if floated free from the national finances, the HRA would be in a similar position to a RSL and the only resources available for stock maintenance and investment would be local HRA resources. If the assumptions about investment needs in the subsidy system prove too low, and actual investment needs are higher, this leads to an unviable business plan. For Salisbury, the difference between the estimated long term maintenance needs of the stock compared to the resources available under the subsidy system may be in the ratio 1.7:1 (£240m vs £140m over 30 years in cash terms).

The crunch issues therefore within the project have been:

- What is assumed in the longer term about the future of subsidy.
- The level of investment resources assumed within the settlement.

The level of allowances within the system is based on:

- Management and Maintenance (M&M) allowances for service delivery
- Major Repairs Allowance for stock investment.

The experiences of the pilot authorities differ on whether service costs are higher or lower than M&M allowances. However, for all authorities, the level of MRA is insufficient in the longer term to maintain the decent homes standard, let alone fund the improvements to the stock necessary for long-term sustainability. Alternative calculations therefore focus on increasing investment in stock over the long term, effectively using the future rental surpluses which are likely to arise within the system.

4.6 Salisbury and self financing: initial thoughts

The future of subsidy is therefore directly related to the future of self financing as what makes self financing more viable involves increasing expenditure allowances made within the subsidy system in the future.

If the subsidy system continues unchanged for 30 years, the current negative subsidy of £7m at Salisbury would rise to over £25m or <u>60% of rent income</u> by year 30. This is amongst the highest future negative subsidy payable that we have seen in our work on the pilot project. Release from the system would involve a ‘buy out’ of future rising surpluses as well as the current position.

Conversely, if the future of negative subsidy was ‘frozen’ at current levels (£7-8m per year), a ‘buy out’ would simply entail replacement of negative subsidy payments with debt charges – akin to taking out a mortgage where repayments are frozen (subject to interest rate fluctuations) whilst income rises.

The latter has been the position argued by the pilot authorities, particularly as the former approach puts an authority in a worse position on day one of self financing than if it had stayed in the system.

It should be recognised however that to be released from a large negative subsidy position, Salisbury’s HRA will need to take on a significant amount of debt. The latter scenario about would be entail a ‘buy out’ of around £100-120m, the interest charges for which would be close to the negative subsidy currently paid out from the HRA and represent a reasonable ‘deal’. The former scenario could result in a much larger ‘buy out’, perhaps over £200m and would therefore not prove viable.

4.7 Self financing and possible next steps

There is a substantial need for long-term investment programme for Salisbury's existing stock. The 3-5 year capital programme is similar to other retention authorities but more investment is needed. The future under the subsidy system can only allow the adoption of an effective long term plan if the volatility and the levels of under-funding, particularly of the Major Repairs Allowance, are addressed in the Subsidy Review.

However the self financing debate moves forward, it is worth reiterating that the HRA business plan forecast at Salisbury reflects the likely worse case scenario and that the outcome of the subsidy review will increase the viability of coming out of the system.

5 Future actions

The council should be able to take advantage of the favourable policy environment for new build housing in the forthcoming period.

A local housing company could be established almost immediately and, providing potentially suitable sites and schemes can be found, initial modelling and development appraisal work undertaken.

The key factors affecting a decision to go ahead are summarise below:

- The availability of land and vacant sites, in fill sites and opportunities for redevelopment within the district,
- The range, type and tenure of properties in priority housing need and the cost of providing them
- The approach to the setting of tenancy conditions and rent levels
- The benefit of existing SDC housing services managing new stock both in terms of consistency and economies of scale with the HRA stock
- Review of financing available within the council and whether an initial approach to the Housing Corporation would be advantageous
- The options for joining partnerships with developers/RSLs to carry out the actual works
- Whether such a company should be charitable or non-charitable.

Newly build HRA properties may benefit from the relaxation of financial constraints when the Housing and Regeneration Bill becomes law and consideration of this approach would also be needed; the main disadvantage being that it is extremely unlikely that HRA properties would attract social housing grant.

For self financing and the subsidy review, the council is best advised to keep a watching brief and consider the ways in which it might present evidence to the review as details of the progress and process emerge in the next few weeks.