ABSTRACT
This report summarises the outcome from an assessment of the long term affordability of the Housing Revenue Account’s 2010/2014 Financial Plan carried out as part of updating the Housing Revenue Account’s 30 year business plan.

1 RECOMMENDATIONS
The Committee is recommended to:-

a) Note the contents of this report for its interest and in particular the key assumptions underpinning the affordability analysis;

b) Note that based on the assumptions made and the affordability analysis undertaken, the 2010/2014 Housing Revenue Account Financial Plan is considered to be affordable, prudent and sustainable as required by the Prudential Code; and

c) Note that the business plan and affordability assessment will be updated as necessary to assess the viability of future Housing Revenue Account capital project proposals.

2 BACKGROUND
2.1 Members will be aware that the Council must comply with the self regulating Prudential Code when setting its capital budgets. The Prudential Code requires the Council to consider the affordability and sustainability of its capital spending plans. This applies equally to the Housing Revenue Account capital plans as it does to the General Fund.

2.2 Prudential Indicators which measure affordability, prudence and sustainability require to be set for 3 forward years as part of the annual budget setting process. This 3 year horizon is however considered insufficient to genuinely assess the long term impact of capital investment decisions.

2.3 Members will also be aware that a 30 year business plan (including capital spend requirements) was developed in conjunction with external advisers (Arneil Johnston) for the Housing Revenue Account (HRA) and members have previously been updated in this regard (report 546/09 refers). Given the limited forward looking time horizon required under Prudential Code reporting arrangements and in recognition that the HRA has a 30 year business plan, it is considered appropriate to evaluate the overall HRA capital affordability position over the longer term and the 30 year business plan has been used as the base for this purpose.

2.4 In this regard, members are asked to note that it has been necessary to base this evaluation on a number of key assumptions such as future levels of expenditure, priority projects, capital receipts, interest rates etc.

2.5 Members should also bear in mind when considering this report, that the Government has the power to limit capital borrowing at both a national and local level and this would
apply across the Council, encompassing both HRA and General Fund. Whilst there has been no indication given that a limit is likely to be imposed in the near future, should such an eventuality arise the HRA’s capital spending plans would require to be reviewed and possibly scaled back.

3 2011/12 LOCAL GOVERNMENT FINANCE SETTLEMENT – CAPITAL FUNDING

3.1 Members are asked to note that unlike the General Fund, the HRA does not receive any loan charges grant support or other capital support through the Finance Settlement details announced by Finance Circular 14/2010 (of 9 December 2010).

3.2 The HRA is a ring-fenced and self financing service of the Council and all revenue consequences from capital expenditure must be met from within the HRA revenue budget funded by the rental income received from the tenants.

3.3 The HRA can however receive some Government capital support from specific funding that the Government may from time to time make available. Such funding must generally be bid for and has recently included Affordable Housing Grant. Any successful bids for such funding effectively reduces the net capital cost of projects to the HRA and as a result the revenue consequences.

4 AFFORDABILITY ANALYSIS

4.1 Starting with an update of the 2010/11 position, the capital affordability analysis which has been undertaken has projected the position over the 30 year period of the business plan (i.e. 2011/12 to 2039/40) for the following:-

- the HRA’s existing loan charges commitments (unavoidable costs);
- estimated levels of HRA capital expenditure;
- estimated levels of capital receipts & other contributions; and
- estimated levels of borrowing.

4.2 This has involved using estimates and making assumptions which will no doubt change over time but the analysis is considered to be both robust and reasonable based on known information at this time.

4.3 Key Assumptions

As with any exercise of this nature the outcomes depend on a number of key assumptions and these are listed below:-

4.3.1 Loan Charges Costs

It is considered that overall loan charges costs should not exceed 25% of the projected rental income in any individual year. This reflects the capital intensive nature of the Housing service as much of the service is focussed on delivering and maintaining housing stock.

The external advisers who assisted with the preparation of the base business plan model have been approached for a view of this assumption. On the basis of their experience in the Housing environment, they are of the view that this assumption is not unreasonable.

The affordability position is therefore based on the premise that this parameter will be met.
4.3.2 Existing Commitments

The cost of principal repayments on existing commitments is known with certainty from the Council’s fixed asset management system.

Assumptions have to be made however in respect of future interest and debt management expenses rates in order to project forward the overall loan charges costs arising from past expenditure and borrowing as well as the anticipated future borrowing levels. In the current austere economic climate, the Council is facing a period where borrowing rates are projected to rise steadily. Accordingly the affordability projections assume that the interest rate on the Consolidated Loans Fund (from which the HRA borrows) will initially rise steadily but will rise more sharply in the later part of the 30 year period. In this regard, the following interest rates have been assumed:-

- 4.70% for 2010/11;
- 4.75% for 2011/12;
- 4.85% for 2012/13;
- 4.95% for 2013/14;
- 5.05% for 2014/15 to 2017/18;
- 5.25% for 2018/19 to 2021/22;
- 5.50% for 2022/23 to 2025/26; and
- 5.75% for each year thereafter.

In respect of debt management expenses, a rate of 0.08% has been applied in all years as this is in line with the average actual expenses rate in recent years.

These rates are considered reasonable and prudent at the present time.

4.3.3 Capital Expenditure

The draft HRA 2010/2014 Financial Plan (appendix 1 to report 113/11 refers) was used as the starting point for making the long term affordability projections described in this report.

The affordability projection requires however to make specific assumptions regarding future capital expenditure and these assumptions need to be made in the context of ensuring that Scottish Housing Quality Standards (SHQS) are achieved and maintained. To this end the following very broad levels of capital expenditure have been assumed beyond the current period of the Financial Plan:

- £6.0m p.a. for 2014/15 and 2015/16; and
- £8.0m p.a. thereafter.

It should be noted that it may be necessary to revisit the assumed levels of capital expenditure in future long term affordability assessments to take account of, amongst other things, the outcome of condition surveys of the housing stock.

Members are asked to note that in addition to addressing SHQS levels, these levels of capital expenditure take account of the loan charges costs parameter set out at 4.3.1 above.

4.3.4 Projects Funded Under Prudential Borrowing

As noted at section 3 above, all revenue consequences from capital expenditure (including financing costs) are met from the HRA rental income stream. In this regard, all borrowing undertaken by the HRA is Prudential Borrowing.
4.3.5 Capital Receipts

The Council has been reasonably successful in generating capital receipts from the sale of Council House over the years. Members have been updated regularly in this regard and it is considered that with the reducing numbers of sellable housing stock, combined with the removal of Right To Buy for new tenancies, the levels of capital receipts attainable in the future will reduce.

To this end the long term affordability assessment assumes that the following levels of capital receipts will be achieved:

- £1.400m for 2010/11;
- £1.000m for 2011/12;
- £0.950m for 2012/13;
- £0.900m for 2013/14 to 2019/20;
- £0.700m for 2020/21 to 2023/24; and
- £0.500m p.a. thereafter.

These capital receipts assumptions are considered to be prudent based on past performance and allow for the currently difficult economic conditions. In the event that capital receipts exceed these estimated levels this will reduce the HRA’s need to borrow or can be used to increase capital expenditure.

4.3.6 Other Contributions

In respect of other contributions, these have only been included where already confirmed (e.g. Scottish Government Affordable Housing Grant or Affordable Housing Revenue Account). Should any additional “other” contributions be secured into the future, these will either be utilised to reduce borrowing or to enhance the capital programme as appropriate at the time, taking on board updated long term affordability assessments, capital requirements or grant conditions.

4.3.7 New Borrowing

As members will be aware it is the level of new borrowing required to fund capital expenditure which determines future commitments in relation to loan charges costs. The affordability projections therefore estimate the level of new borrowing required after taking into account all of the other assumptions about capital expenditure, capital receipts, etc. and this in turn has been used to calculate estimated loan charges costs into the future. These costs have been projected on an annuity basis and the interest rates detailed under Existing Commitments at paragraph 4.3.2 above have also been applied in estimating the costs of new borrowing.

4.3.8 CFCR

Members will be aware that the HRA revenue budget habitually contains a significant budget to fund capital expenditure directly from revenue resources (CFCR). The long term affordability assessment starts from the premise that no CFCR is initially allowed for in the expenditure calculation, however this results in a significant net income position in each year within the model. This net income is then fully applied to fund capital expenditure prior to determining borrowing requirement levels relative to the assumed capital expenditure levels.

For information, members are asked to note that the CFCR applied in the model averages £5.000m per annum over the 30 year period of the assessment.
It is also worth highlighting that the CFCR resources could if required be used to meet additional borrowing costs to fund a higher level of capital should this be a policy direction chosen. The use of CFCR in this way would however commit resources over the longer term and therefore only provide one-off boosts to expenditure at a time.

4.3.9 Expenditure Slippage

As expenditure slippage is not a capital funding source but merely affects the phasing of expenditure, no slippage assumptions have been included for the purposes of this affordability assessment.

4.3.10 Inflation

With the exception of the period of the Financial Plan (which is stated on an outturn basis), the affordability analysis does not make specific allowance for the effects of inflation, e.g. on capital expenditure on the basis that this is highly unpredictable over time. Whilst this will mean that the true purchasing power of the assumed capital expenditure total into future years will gradually be eroded, members are asked to note that inflation has also been ignored in relation to capital receipts, over the period of the analysis. The affordability analysis therefore ignores the effect of inflation on both the expenditure and funding side.

4.3.11 New Build Housing

The HRA Financial Plan presented at Appendix 1 to the rent setting report (113/11) contains projects to build 83 new Council Houses in Angus and these have therefore been included within the long term affordability assessment.

In addition, members will recall Committee Report 894/10 entitled “Survive and Thrive – Further Housing Contribution” which was noted and approved at the Strategic Policy Committee on 7 December 2010. The report indicated that positive discussions with developers were taking place preparing to unlock sites for Affordable Housing development across Angus. No specific provision for these proposals have been identified in the 2010/11 to 2013/14 Financial Plan, however once specific proposals are known the financial implications of these will be fed through the long term affordability and Business Plan model. The inclusion of such proposals will however be financially neutral to the HRA as the revenue consequences will be funded from the £234,000 savings identified in report 894/10. The non-inclusion of these projects is not therefore detrimental to reaching a conclusion on the outcomes from the long term affordability assessment.

Members are also asked to note that the Tenants Movement have called for a debate on the use of the Housing Revenue Account and new build housing. Tenants, like members, are aware of the need for new Council housing and following this year’s rent setting meeting arrangements will be made to begin next year’s option appraisal as soon as possible with Members being kept fully briefed on tenant’s views. In this regard the updated long term affordability and business plan model will be utilised to assess the viability of any proposals which may arise from this debate.

5 AFFORDABILITY ANALYSIS - OVERALL SUMMARY POSITION

5.1 The affordability analysis brings together a large volume of data and makes a number of assumptions. Table 1 below summarises the key figures in this regard for the current year (2010/11) and forward 3 years (2011/12 to 2013/14) and at intervals of 5 years thereafter.
### TABLE 1 – AFFORDABILITY ANALYSIS – SUMMARY POSITION

<table>
<thead>
<tr>
<th></th>
<th>10/11 £m</th>
<th>11/12 £m</th>
<th>12/13 £m</th>
<th>13/14 £m</th>
<th>17/18 £m</th>
<th>22/23 £m</th>
<th>27/28 £m</th>
<th>32/33 £m</th>
<th>37/38 £m</th>
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<tbody>
<tr>
<td>Capital Expenditure</td>
<td>8.541</td>
<td>12.154</td>
<td>11.690</td>
<td>7.335</td>
<td>8.000</td>
<td>8.000</td>
<td>8.000</td>
<td>8.000</td>
<td>8.000</td>
</tr>
<tr>
<td>Estimated Borrowing</td>
<td>2.507</td>
<td>6.670</td>
<td>5.545</td>
<td>1.305</td>
<td>2.565</td>
<td>3.687</td>
<td>0.028</td>
<td>0.377</td>
<td>0.000</td>
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<tr>
<td><strong>Expenditure :-</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(A) Loan Charges</td>
<td>2.063</td>
<td>2.257</td>
<td>2.392</td>
<td>2.717</td>
<td>3.368</td>
<td>5.003</td>
<td>4.973</td>
<td>5.154</td>
<td>4.151</td>
</tr>
<tr>
<td>Other Income</td>
<td>1.966</td>
<td>1.956</td>
<td>1.971</td>
<td>1.986</td>
<td>2.039</td>
<td>2.094</td>
<td>2.151</td>
<td>2.211</td>
<td>2.275</td>
</tr>
<tr>
<td>Net Income (D) – (B)</td>
<td>5.131</td>
<td>4.484</td>
<td>4.164</td>
<td>4.078</td>
<td>4.463</td>
<td>3.611</td>
<td>4.574</td>
<td>5.391</td>
<td>7.401</td>
</tr>
<tr>
<td>Affordability Check (A) / (C)</td>
<td>11.0%</td>
<td>11.9%</td>
<td>12.5%</td>
<td>14.1%</td>
<td>16.8%</td>
<td>24.2%</td>
<td>23.1%</td>
<td>23.0%</td>
<td>17.8%</td>
</tr>
</tbody>
</table>

**Notes To Table 1**
1. Paragraph 4.3.8 above notes that the net income is fully applied as CFCR in the affordability model, however members should note that in the case of 2010/11, the net income of £5.131m comprises both CFCR of £4.634m and the projected current year surplus of £0.497m.
2. Some differences arise in the numbers presented above for 2011/12 as the affordability model treats bad debt provisions and income from service charges differently from the presentation in appendix 2 to the rent setting report (report 113/11 refers), however the net income position is maintained.

5.2 The analysis shows a projected peak in new borrowing levels over the years 2011/12 and 2012/13 - this is largely the result of the borrowing projected to be required in respect of new 83 build properties in Arbroath, Montrose, Kirriemuir, Carnoustie and Monifieth.

5.3 The analysis also shows that the affordability check against the 25% parameter set at 4.3.1 above is not breached, meaning that the projected loan charges costs arising from the projected levels of borrowing are affordable. In this regard and in light of Table 1 not reflecting all 30 years of the analysis, it is confirmed that the model projects that the affordability check does not breach the 25% parameter in any of the 30 years.

5.4 Members will note that the summary in Table 1 indicates that the estimated borrowing requirement reduces considerably in the later years. This reflects a projected increase in the use of CFCR as a consequence of reducing loan charges in respect of debt maturing before the end of the analysis period.

6. **OVERALL CONCLUSIONS FROM AFFORDABILITY ANALYSIS**

6.1 A number of conclusions can be drawn from the affordability analysis which has been carried out. The affordability analysis is however based on a number of assumptions regarding future interest rates, capital expenditure and receipts levels, and capital projects being delivered in line with expected timescales and costs. The analysis
6.2 Despite this risk the Head of Finance believes that the assumptions which have been made are robust, reasonable and prudent for the purposes of informing the Council’s decisions. Critically the analysis confirms that the HRA capital spending plans can be regarded as affordable, prudent and sustainable in line with the requirements of the Prudential Code.

7 **FINANCIAL IMPLICATIONS**

7.1 There are no financial implications arising from this report beyond those outlined in the main body of the report.

8 **HUMAN RIGHTS IMPLICATIONS**

8.1 There are no human rights implications arising from the recommendations in this report.

9 **EQUALITIES IMPLICATIONS**

9.1 The issues dealt with in this report have been the subject of consideration from an equalities perspective (as required by legislation). An Equalities Impact Assessment is not required.

10 **CONSULTATION**

10.1 The Chief Executive and Head of Law & Administration have been consulted on this report.

11 **CONCLUSION**

11.1 This report summarises the outcome from the assessment of the long term affordability of the HRA Financial Plan. Whilst the analysis is based on a number of assumptions given the timescale over which the projections are based, the outcomes are considered to give a reasonable indication of the affordability of the intended HRA capital expenditure programme. The results of this exercise indicate that the 2010/2014 HRA Financial Plan is affordable, prudent and sustainable as required by the Prudential Code.

<table>
<thead>
<tr>
<th>Ron Ashton</th>
<th>Colin McMahon</th>
<th>Ian Lorimer</th>
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</thead>
<tbody>
<tr>
<td>Director of Neighbourhood</td>
<td>Director of Corporate</td>
<td>Head of Finance</td>
</tr>
<tr>
<td>Services</td>
<td>Services</td>
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</tbody>
</table>

**Background Papers** :- No background papers, as defined by Section 50D of the Local Government (Scotland) Act 1973, were used in the preparation of this report.