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Inquiry into Prudential Borrowing and innovative approaches to capital funding

Response from Chartered Institute of Housing Cymru

RE: A call for evidence – Prudential Borrowing and innovative approaches to capital funding

Thank you for the opportunity to provide evidence to the National Assembly's Finance Committee to help inform your inquiry into the use of prudential borrowing by Welsh local authorities and other organisations and innovative approaches to capital funding.

The Chartered Institute of Housing is the only professional organisation representing all those working in housing. Its purpose is to maximise the contribution that housing professionals make to the well being of communities. In Wales, we aim to provide a professional and impartial voice for housing across all sectors to emphasise the particular context of housing in Wales and to work with organisations to identify housing solutions.

Prudential borrowing for housing investment

The Chartered Institute of Housing in Cymru is extremely supportive of the need to ensure that local authorities who have retained their housing stock are able to access the resources necessary to meet the needs of their tenants and deliver the Welsh Housing Quality Standard (WHQS). We believe there is a strong case for enabling authorities to further access resources to assist in regeneration, redevelopment and the delivery of new social and affordable housing.

Along with the Major Repairs Allowance and capital receipts, prudential borrowing offers authorities a potential source of finance to help deliver a sustainable existing housing stock as well as bring forward

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Y Sefydliad Tai Siartredig yng Nghymru,
4 Tŷ Purbeck, Cilgant Lambourne,
Parc Busnes Caerdydd, Llanisien, Caerdydd CF14 5GJ

Ffôn: 029 2076 5760 **Ffacs:** 029 2076 5761
Ebost: cymru@cih.org

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Ymgofforwyd gan Siarter Brenhinol Elusen Gofrestredig rhif. 244067/R

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www.cih.org/cymru

Chartered Institute of Housing Cymru,
4 Purbeck House, Lambourne Crescent,
Cardiff Business Park, Llanishen, Cardiff CF14 5GJ

Tel: 029 2076 5760 **Fax:** 029 2076 5761
Email: wales@cih.org

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new schemes to enhance housing supply and conditions. A key feature of prudential borrowing for housing purposes is that the borrowing can be directly linked to a tangible asset that, providing it is maintained in a sustainable way, will raise rent income which can be utilised to service borrowing over the long term.

CIH has long argued for a reclassification of housing borrowing in line with most European countries as outside of the Public Sector Net Debt enforced as the major fiscal measure by UK Government. This would enable local authorities to raise housing borrowing against future rental streams without scoring against mainstream taxation totals in the public accounts and place local authorities in line with housing association colleagues. We recognise, however, that current political, financial and economic conditions make such a reclassification impossible in the short to medium term.

We would however maintain that borrowing for housing purposes is materially different to many other forms of borrowing undertaken by local authorities. This is exemplified by the scale and nature of borrowing undertaken since the introduction of the Prudential Code in 2004 and the relationship with the level of supported borrowing contained within the HRA Subsidy (HRAS) system.

The HRAS captures rental surpluses from local authorities and pays these over to UK government in line with a methodology and formulae established under the 1989 Local Government and Housing Act. Contained within the surplus calculation is a measure relating to historic housing debt supported in the system. If an authority has high debt, the surplus will be lower and vice versa. The current overall surplus is £73m for 11 authorities with stock (commonly referred to a negative subsidy) and this provides for historic supported housing debt of £307m. Annual HRAS determinations affect the level of supported housing debt by reducing it for an amount of Minimum Revenue Provision and the set aside of 75% of Right to Buy receipts.

Since 2004, a majority of stock retaining authorities have elected to borrow above the level of supported housing debt in support of their capital programmes, and in particular towards meeting WHQS. Across the country, the level of borrowing has been well over £100m. Interest charges relating to this additional borrowing are being supported from the rental income collected and demonstrate the inherent sustainability of borrowing linked to a predictable rental stream.

A major potential constraint in delivering more levels of investment arises as a result of the HRAS capturing rental surpluses for return to UK government. We are working closely with Welsh Government in supporting the dialogue with Treasury around ending the HRAS through a one-off settlement along the lines being implemented in England. This is likely to involve local authorities taking on more debt in lieu of making future negative subsidy payments. If released from the system future rental surpluses could then be harnessed to support investment in the housing stock and services. One option for authorities might be to borrow against these surpluses to further enhance investment. A key component of abolition would be the ending of supported debt so that all housing borrowing became unsupported or 'prudential'.

However if, as seems likely, UK government insists on some form of restriction of borrowing for housing purposes in future (as they have in England to avoid excessive additional public sector debt), this might lead to a position where local authorities may not be able to deliver investment that could be sustainable and affordable from future income streams into the future.

It is therefore vital that the ending of HRAS and terms of any settlement are carefully constructed so as to allow local authorities to bring forward investment appropriate to meet WHQS and regeneration / build programmes and not to unduly restrict authorities in meeting the objectives set by Welsh Government.

We would argue for a settlement that allows some degree of flexibility around additional prudential borrowing, which might be linked to the achievement of Welsh Government objectives. Sustainable housing business plans could be developed for all authorities with long term management of debt as a key financial toolto achieve long term objectives; prudential borrowing would therefore be a bedrock upon which the long term sustainability of council housing could be developed.

The impending implementation of council housing self financing in England has led to most councils developing business plans which have additional investment in regeneration and new supply at the heart of their plans. In the short term, this may not be significant in terms of numbers but offers an insight into the potential for business plans to deliver housing led regeneration.

Housing prudential borrowing could offer similar prospects in Wales in a self financing context. Free from the HRAS and with an appropriate level of settlement, local authorities could offer a significant contribution to wider regeneration, in the same manner as that being delivered by stock transfer housing associations.

Other models for investment

The housing sector also offers a unique experience in the delivery of private finance through traditional and stock transfer housing associations. The commitment of nearly £50m of dowry funding by Welsh Government to support 11 stock transfers have allowed significant levels of private finance to be levered in to meet WHQS, support regeneration, and potentially deliver new build programmes in the long term.

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Housing associations offer the potential to bring private finance to support the development of public sector assets in the context of securing value for money on asset transfer. It is likely that models involving the transfer of local authority or any other public sector land for development by housing associations will continue to be a significant option for ensuring new housing is developed in the right places.

The Localism Act in England will create potential greater diversity in models of tenure and rent setting for social and affordable housing. Rent levels may be set higher to allow greater leverage of private finance borrowing thereby reducing capital grant subsidies from the exchequer.

Concerns remain however over the potential for such models of greater leverage to deliver over the long term, especially given the current and likely future constraints in the private finance markets. Banks have retrenched significantly and are looking to renegotiate loan books across the housing association sector. Therefore, whilst there is scope for further leverage, it is likely that facilities will be maxed out for many developing associations.

In this climate, perhaps there needs to be a fresh look at opportunities for public/private partnerships around housing delivery. Options such as Real Estate Investment Trusts for affordable housing are at an fledgling stage across the UK. New and diverse models of cross subsidisation involving market renting are also likely to form part of the debate.

We hope this information has been useful to the Committee in progressing its inquiry and we would of course be happy to provide further information or clarification on any of the issued raised.

Yours sincerely

V. Hiscocks

Victoria Hiscocks
Policy and Public Affairs Manager, CIH Cymru

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