

Briefing Paper

RESOURCE ACCOUNTING AND THE HOUSING REVENUE ACCOUNT

Adrian Waite – July 2004

Why must all local authorities keep a Housing Revenue Account?

Any organisation needs to keep a record of expenditure and income. Local authorities have a greater need to account for their income and expenditure because they are dealing with public money.

The Housing Revenue Account records expenditure and income relating to council houses and the provision of services to tenants. This includes management and the repair and maintenance of stock and the rent and income from other sources such as housing subsidy.

On 1st April 1990 the then government introduced a new 'Housing Finance Regime'. This defined what transactions should be recorded in the Housing Revenue Account, and enabled the government to influence directly the finances of local authority housing. A 'New Housing Subsidy System' achieved this. This subsidy system has continued until the present day, although successive governments have modified it.

The legal requirement to keep a Housing Revenue Account

The legal position is set out in Part VI of the Local Government and Housing Act 1989, which requires local authorities to -

- Prepare a Housing Revenue Account showing certain debits (costs) and credits (income) and make it available to the public.
- Keep the budget under review.
- Take all reasonable practical steps to avoid a deficit on the account.

Authorities maintain Housing Revenue Account balances – made up of surpluses that have been carried forward from previous years. An authority can make a deficit in a particular year, but it cannot make a cumulative deficit. The Act specifies what a local authority can charge to its Housing Revenue Account and what income can be credited there. This requirement creates the "ring fence".

Plus Appropriations

Revenue Contributions to Capital

Transfer to Major Repairs Reserve (where depreciation is lower than the Major Repairs Allowance)

Transfer from Major Repairs Reserve (where depreciation is higher than the Major Repairs Allowance)

Minimum Repayment Provision

Equals Surplus/Deficit for the year

Plus Surplus at beginning of year

Equals Cumulative Surplus/Deficit at the end of the year

The following notes describe what these items contain in more detail.

Expenditure

Repair and Maintenance

This includes the cost of maintaining the Council's housing stock including the management of the maintenance function. 'Maintenance' includes repainting, responsive repairs and planned maintenance. It does not include major repairs - for example, replacement bathrooms, electrical rewiring or re-roofing.

Management Expenses

General Expenses refer to costs relating to the whole housing stock or all tenants. It includes rent collectors, costs of letting properties, most of the management of the Housing Department, computer costs and support costs such as accountancy and legal.

Special expenses apply to only some of the tenants. They include cleaning communal areas of flats and maintenance of open spaces. The government is encouraging local authorities make a service charge to recover some or all of this expenditure. Support costs relating to sheltered accommodation have been met from the General Fund and financed by Supporting People Grant from 2003/2004.

Rents, Rates, Taxes and other charges

This includes rents, rates, leases and Council Tax paid in respect of empty council houses waiting to be re-let or for property used to provide services to tenants.

Rent Rebates (Housing Benefit for Council Tenants)

Some tenants are able to claim Housing Benefit because of their limited means. As a result they have their rent reduced. This is a Rent Rebate and the total cost of these is charged to the Housing Revenue Account. From April 2004 this will no longer be a charge to the Housing Revenue Account.

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Transfer of Negative Subsidy Surplus

This applies where an authority has a surplus on its 'Notional' H.R.A and is therefore obliged to transfer that amount to the government.

Transfer to Housing Repairs Account

Some authorities operate a 'Housing Repairs Account'. In these cases, expenditure on Repairs and Maintenance is charged into the 'Housing Repairs Account' rather than directly to the 'Housing Revenue Account'. The 'Housing Revenue Account' makes transfers to the 'Housing Repairs Account' so that the account is in funds. Any surplus on the 'Housing Repairs Account' can be carried forward to the following year, or transferred back into the 'Housing Revenue Account' (see below).

Transfer to a DLO / DSO Trading Account

Under the 'Best Value Accounting Code of Practice' any significant profit or loss by a DLO or DSO (an in-house trading unit providing services such as building maintenance) is apportioned to the account that received the service that made a loss. This is to ensure that the 'true' cost of providing services is reflected in the accounts.

Provision for Bad or Doubtful Debts

Local authorities are usually owed significant amounts in arrears of rent or other income. Sometimes this income is uncollectable and has to be written off. It is good accounting practice to make a provision for such bad or doubtful debts.

Cost of Capital

This was introduced as part of Resource Accounting. It reflects the 'true' cost to the local authority of its investment in the housing stock. To calculate the 'Cost of Capital' an authority values its housing stock and multiplies this figure by 3.5%.

Before this, local authorities charged the Housing Revenue Account with 'Capital Financing costs'. These included repayment of principal and interest on loans that the local authority had taken out to finance capital expenditure. This system was criticised because where there was no debt outstanding on a property there was no 'Capital Financing cost'.

The 'Cost of Capital' is considered to reflect the 'opportunity cost' incurred by the authority because of its own investment in council housing, as well as the actual cost of the loans outstanding. However, 'Cost of Capital' is not a real cost to the local authority, and so it is paid into the 'Asset Management Revenue Account'. The local authority does still have to pay the capital financing costs. The 'Asset Management Revenue Account' meets these. How this works is considered below.

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Depreciation

Depreciation was introduced as part of Resource Accounting. It represents the reduction in the value of assets over time. It is often calculated on the same basis as the 'Major Repairs Allowance' although the Audit Commission are increasingly suggesting that authorities do a separate calculation that tends to be higher than the Major Repairs Allowance in the south and lower in the north. It is not a real cost to the local authority and so is paid into a 'Major Repairs Account'. The calculation of the 'Major Repairs Allowance' and the operation of the 'Major Repairs Account' are considered below.

Income

Rents from Dwellings

This includes rents collected from the letting of council housing.

Rents from Other Property

This includes rents collected from garages and shops on council estates.

Service Charges

This includes any other charges made, including heating, cleaning, welfare services and payments by leaseholders. Leaseholders are ex-tenants who have bought their council flat on a leasehold basis.

Contributions towards Expenditure

This includes payments from social services authorities and income from rechargeable repairs. Where benefits or amenities are shared by the whole community the General Fund makes a contribution towards the cost.

Transfer from the Housing Repairs Account

A local authority that keeps a Housing Repairs Account (as described above) can transfer surpluses on that account into the Housing Revenue Account.

Reduced Provision for Bad or Doubtful Debts

If there is a provision for bad or doubtful debts it can be reduced and the balance transferred to the Housing Revenue Account.

Transfer from DLO / DSO Accounts

There is a requirement to transfer the profit of a DLO or DSO on housing work to the Housing Revenue Account where the profit is significant (see above).

Housing Revenue Account Subsidy Receivable

This is the amount due from the government in respect of Housing Revenue Account Subsidy. The calculation of this sum is considered in a separate briefing paper.

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Operating Expenditure

Adjusting Transfer from Asset Management Revenue Account

The Asset Management Revenue Account for the Housing Revenue Account was created as part of the introduction of Resource Accounting. The account receives the 'credit' for the 'Cost of Capital' charge. It also pays the Capital Financing Costs. In most local authorities, the 'Cost of Capital' is greater than 'Capital Financing Costs' and so the Asset Management Revenue Account makes a 'profit'. This 'profit' is then transferred into the Housing Revenue Account as an 'Adjusting Transfer from Asset Management Revenue Account'.

The figure in the AMRA is reduced by the amount of any investment income received on capital receipts that are "set aside" as provision for debt repayment. For most authorities interest is charged on this net figure of principle outstanding because it is assumed that "set aside" receipts can be used to repay debt. The interest rate is the Consolidated Rate of Interest, which is calculated in accordance with Government determinations.

Interest Payable on Overdrawn Revenue Balance

If cash is overdrawn in the Housing Revenue Account on average throughout the year, it will incur interest charges. While a local authority will not normally have a separate bank account for the Housing Revenue Account it must calculate the amount of interest to be charged (if any) as if it has.

Interest Receivable

- a) Interest on Capital Receipts - authorities receive this (sometimes called the 'item eight credit') where the amount of capital receipts invested is greater than the level of loans outstanding.
- b) Interest on Mortgages in respect of sold council houses
- c) Other Interest Receivable - There is a credit to the Housing Revenue Account where the average cash balance throughout the year is in surplus.

Appropriations

Revenue Contributions to Capital

Revenue Contributions to Capital are where a local authority uses revenue resources to finance capital expenditure.

Transfers to and from the Major Repairs Reserve

The Major Repairs Allowance is paid to local authorities as part of Housing Subsidy – and its calculation is considered below. It is designed to provide authorities with sufficient funding to keep their stock in a 'decent' condition on an ongoing basis.

The accounting process is for a local authority to receive Major Repairs Allowance as part of its Housing Subsidy, and to use this to meet depreciation costs. These are then paid into the Major Repairs Reserve. The Major Repairs Reserve is then used to fund Major Repairs. If the level of depreciation is the same as the level of the Major Repairs Allowance, the Major Repairs Allowance is effectively 'ring fenced' to Major Repairs.

As the government wants local authorities to use all the Major Repairs Allowance to fund Major Repairs, it wished to achieve this by obliging local authorities to use the calculation of the Major Repairs Allowance to calculate depreciation.

However, accountants argued that local authority chief financial officers should determine the level of depreciation to charge. The result was a compromise where the government said that local authorities could calculate depreciation on a different basis from the Major Repairs Allowance. But, if they did so, they would have to justify this in the accounts and would have to make a transfer to or from the Major Repairs Reserve to bring the net transfer to the Major Repairs Reserve back to the level of the Major Repairs Allowance. As a result the government achieved its intention of 'ring-fencing' the Major Repairs Allowance to Major Repairs.

Conclusion

The new format of the Housing Revenue Account that has been introduced with Resource Accounting makes presentational changes rather than substantive changes. This is because the items that are charged or credited to the Housing Revenue Account remain the same, and the effect on the bottom line – the Housing Revenue Account balances – is neutral. However, the government has obliged local authorities to calculate the 'Net Cost of Services that in the government's view – reflects the 'true cost' of the provision of council housing.

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