Durham County Council

Housing Options Appraisal
Financial Report

FINAL REPORT
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Executive Summary

ConsultCIH was appointed by Durham County Council to support its housing options appraisal with a detailed financial analysis of the options open to the council for the future management and ownership of its stock. Summary conclusions from our analysis are set out below.

Self financing for Durham – the baseline plan

The HRA self financing business plan highlights shortfalls of capital resources against spending needs of £63m over 10 years, which is 16% of total needs in that period. Whilst the plan can generate sufficient resources to meet needs over 20 years, the council might consider that the deferral of this amount of investment over such an extended period is untenable.

£100m of debt would be outstanding after 30 years which would need to be addressed if the plan is to demonstrate long term viability – this suggests a need for a further £2m savings over and above the £3m annual efficiencies included in the baseline plan.

The central issue is therefore that the operation of the debt cap under self financing is incompatible with the up front nature of the investment needs. A solution is therefore needed which enables the council and providers to achieve the full investment profile in all years.

An analysis of the individual plans for each provider area shows that the viability of each would be completely dependent on the allocation of debt settlement between three sub-plans. There are such wide potential variations in the allocation of debt between areas that the analysis feels rather an academic exercise. As time moves on, it is less likely that the formulae bases for the former subsidy allowances will continue to apply robustly to the stock in each area.

What would be needed to make self financing work for Durham

In order to balance the plan to zero debt at the end of year 30 would require additional annual savings of up to £2m. The cumulative need for efficiencies would therefore be in the region of £5m pa against current revenue spending of £30m. Capital shortfalls would however remain - £43m for the first 10 years.

Alternative approaches might include reducing capital profiles through active asset management.

Provider costs and support services

Unit costs vary between providers and between them and the council; there is evidence that these reflect the allowances from the HRA subsidy system that applied to the three former districts. This might suggest that further forms of analysis could be aimed at targeting efficiencies between providers.

There are £5.3m of budgets for support services out of a gross management cost of c£17m and gross service revenue cost of £32m in the HRA. This total represents around 15% of total costs and 30% of management costs. Whilst these might not appear to be on the high side for local authority housing services, the scale of the support and central costs might suggest that there is scope for efficiencies through rationalisation.

Traditional stock transfer (LSVT)

The financial landscape for traditional LSVT has changed significantly and transfer can now only proceed on the basis that expenditure assumptions are in line with those made under self financing.

Taking into account the receipt of decent homes backlog funding and the potential to claim a VAT shelter for 15 years, a maximum transfer valuation for the whole stock would be c£56m.

This compares to a potential reduced debt position of £150m upon transfer leaving a gap of c£94m to be bridged.

Whilst funding towards this gap could be identified across the council, a purchasing housing association or changing the basis upon which private finance is made available under LSVT, these sources are unlikely to bridge the whole gap. The council would need to mount an argument to government seeking additional debt write off on transfer based on a value for money and efficiency case around the timing and effectiveness of investment.

The government is due to update its transfer guidance in the autumn of 2011 which might set out the basis upon which it might consider such a case post-self financing.

At the provider level, a transfer for East Durham would require dowry funding. For Durham City and Dale & Valley, although positive, transfer of these two would leave the remaining HRA with too high a debt to sustain unless further debt write off from government could be secured.

Stock transfer via a Council/Community (CoCo) organisation

The Council/Community (CoCo) company model might have merit in Durham given that the financial pressures in the business plan are in part caused by the constraints of the HRA borrowing cap.

The CoCo model could allow private finance borrowing to meet needs above the cap which could then be repaid during the lifetime of the business plan. At the whole stock level, this could total less than £50m on the basis of a £66m reduction in HRA debt on transfer to the CoCo. The debt reduction would be subject to negotiation with government but indications are that such a reduction would be achievable.

As with the self financing plan, however, additional year on year efficiencies over and above those included in the current MTFS would be required in order to achieve viability.

At the provider level and from a purely financial perspective, the CoCo model might in principle apply most usefully in the East Durham context where spending pressures are the greatest in the early years. Pursuing a CoCo model for East Durham might suggest a reduction in HRA debt of c£30m although this would be subject to negotiation with government.

The CoCo model is at yet untried at any authority – there are known to be three ALMO authorities interested in engaging government around the option.

Overall conclusions

There are challenges affecting each of the main options for Durham.

For self financing, the debt cap is a key constraint in meeting backlogs of investment and even further efficiencies would not eliminate capital shortfalls. For stock transfer, values are low and a strong value for money case would be required to government to secure debt write off. For CoCo, further efficiencies would also be required.

In addition to the delivery of £3m of efficiencies already included in the council's financial strategy, it is unlikely that the providers can avoid the need to secure further efficiencies in order to deliver a sustainable business plan under any of the options. These could be delivered through a combination of revenue service rationalisation and support service sharing, reduction in capital spending needs and proactive asset management to reduce future maintenance liabilities.

Should the outcome of the appraisal be to pursue long term private finance options, the timing of the delivery of these is likely to be affected by the need to negotiate with government over a possibly lengthy period.

Whilst there are options for delivering different solutions for each of the provider areas, our analyses tend to suggest that the council might find it advantageous to seek a single type of ownership and management solution, albeit split into one, two or three providers. To that end, work can proceed towards the delivery of efficiencies in advance of the delivery of long term solutions, particularly as existing financial strategies require significant efficiencies to be delivered from 2012 onwards, with a view to implementing the preferred option in 2-3 years.

1 Introduction

1.1 Background and methodology

ConsultCIH was appointed by Durham County Council to support its housing options appraisal with a detailed financial analysis of the options open to the council for the future management and ownership of its council housing stock.

The council has adopted a traditional and comprehensive approach to the delivery of the appraisal, with the establishment of a Steering Group of residents, members, staff representatives and advisers to oversee the project and charged with providing a recommendation to the council on preferred options for the future.

Reports from the council and other advisers set out in detail the processes that have been undertaken, the approach to consultation with the wide range of stakeholders that have been engaged to date and the outcomes of the overall appraisal that the Steering Group have arrived at. The objective has been to secure a decision on the preferred way forward by the council in December.

This report is therefore focused specifically on the financial analyses supporting the appraisal, setting out the financial factors, issues and implications for each of the options under consideration. In parallel, a report from our partners Savills addresses a detailed analysis of stock and asset performance.

The work set out in this report draws upon previous work we have undertaken with the council in assessing the implications of Housing Revenue Account (HRA) reform for the HRA business plan – towards the end of Mach this year, the business planning process had concluded that the council was likely to face financial issues in delivering its preferred levels of investment following the implementation of self financing.

Our methodology has been as follows:

- Develop a financial model for HRA self financing to test the financial implications of the ‘as is’ situation – we term this the ‘baseline’ model throughout this report
- Develop financial models for alternative ownership options (including stock transfer)
- Analyse the overall costs of service delivery and how these split between ‘front line’ and ‘overheads’
- Prepare presentations summarising the financial findings at all stages and delivering these to the Steering Group, the HRA Board and other forums so as to deliver information and receive feedback
- Make a presentation to the Steering Group Jury session held on 24th June 2011.

Throughout, we have worked closely with officers from the council and the three housing management providers and would like to thank all who have been involved in developing the financial analyses up to this point.

It should also be noted that we have separately provided an updated business plan model for the council to assist it in the development of the actual plan for self financing and trained finance officers in the use of the model so that they can support the business planning, budget and financial strategy preparations that will be needed between now and self financing 'go live' in April 2012.

1.2 Introduction to this report

This report summarises the work that has been undertaken in the appraisal. There have been several iterations of the financial analyses since the project began and this report sets out the position as at October 2011. Readers are directed to the series of presentations made to the Steering Group, HRA Board and other stakeholder events which accompany the analysis within this report.

As the project enters the autumn of 2011, the process of determining next year's budgets for the HRA and HRA capital programme is beginning and there will necessarily be updates to the assumptions made around rents, income, management, maintenance and major repairs. The final draft HRA settlement is due to be published on or before 11th November.

The process of option appraisal does not obviate the need to set budgets and to begin the process of delivering the efficiencies that have already been identified as necessary under the existing Medium Term Financial Strategy (MTFS).

It will be important for the council to ensure that, as budgets are set for 2012.13 and the MTFS is updated, there is a suitable process adopted for updating of the outputs in the modelling that supports this report and that, as far as possible, there is wide understanding amongst stakeholders as to the reasons why outputs move on and how assumptions change over time.

A report has been prepared by the council's finance officers for discussion by the Cabinet in late October 2011. This report updates of the assumptions and outputs around self financing following a review session held between ourselves and officers in late September. Having been given the opportunity to review a draft of the report, we are comfortable that this report provide consistency and continuity with the financial analysis contained within the appraisal project.

2 The options under consideration and the financial analyses

2.1 Introduction to the options

The appraisal process within Durham is complex. The options are in multiple dimensions and affected by key local factors, including:

- The combination of two ALMOs and one in-house provider, in a new unitary where the finances are continuing to bed down at a challenging financial time

- One ALMO area (East Durham) with a significant unmet backlog of decent homes works, despite the recent announcement of funding from government.
- The other ALMO area (Dale and Valley) having completed decent homes works and now looking ahead to tackling wider issues of sustainability
- The in-house area (Durham City) with refurbishment backlogs highlighted by a recent history of lower funding than the other two areas
- The different standards of refurbishment that may have applied in the three former district areas
- Significant issues with stock design and property types across some areas of the stock
- Relatively low values of land and dwellings in many parts of the county limiting the opportunities for regeneration and redevelopment.

Conversely, the diversity of experiences and factors offer some opportunities for rationalisation of management operations across the three areas as well as moving towards a more consistent set of standards across the county.

Our work (supported by Savills) has therefore focused on assessing the options for future management and ownership in three dimensions.

These dimensions are 1) how many providers, 2) who owns the stock (council or provider) and 3) the stock itself (in asset management terms).

2.2 Financial assessment of provider numbers

Whilst it is too early for a detailed consideration of the number of providers and how financial savings and efficiencies might be delivered through rationalising management structures and the number and coverage of providers, we have undertaken some preliminary analysis of the costs of service delivery between the areas and set out some thoughts about options for rationalisation which might merit further detailed investigative work.

The providers themselves, along with stakeholders across the county, also have their views about the governance, management and delivery mechanisms that are currently in place and which could be developed.

At this stage, we have confined our analysis to:

- A comparison of overall costs against resources across the HRA and the stock

- An initial analysis of the total 'back office' or 'support service' costs that are being incurred between the three providers and the council, with some pointers as to the financial issues that arise.

2.3 Financial assessment of self financing and stock transfer

The majority of our work has been focused on developing the financial models to support analysis of:

- The ‘status quo’ self financing business plan, with assumptions based on known factors from government, with no change to the current pattern of providers (two ALMOs and one in-house provider)

- How the status quo might need to change, financially, in order to deliver a more sustainable business plan

- The financial issues and implications of a more traditional stock transfer to housing associations, created out of the existing providers

- The financial issues and implications of the Council/Community Company (or CoCo) model involving transfer of stock to providers with the retention of (a reduced) HRA debt.

The approaches to CoCo are affected by the fact that this is, as yet, an untried option and engagement with government has only recently begun following the research report published by the National Federation of ALMOs in the spring.

Approaches to stock transfer are affected by the implementation of self financing and it is already evident from those authorities wishing to pursue traditional stock transfer that the government has fundamentally changed the terms of engagement around the financing of stock transfer in the light of the self financing settlement. It is now impossible for any or all of the providers to pursue stock transfer on the sort of financial terms seen elsewhere in the county.

2.4 Asset management analyses

Savills have undertaken a preliminary piece of work around developing a detailed analysis of the asset base, split into archetypes and areas and covering a Net Present Value methodology in assessing the performance of assets.

To an extent, this work stands alone as many of the issues associated with some areas of the stock require addressing irrespective of whether the stock transfers and irrespective of the number of providers.

We understand that further work has been commissioned by the council to drill down further into areas identified within the initial analysis.

2.5 Option combinations

Throughout all of the modelling that we have developed for this project, we have ensured that all of the analyses around management and ownership options are able to be interrogated at the ‘provider’ level. This has enabled us to identify potential workable combinations of provider numbers in different option contexts in order to report an overall position for the council.

The potential combination of options is very large, particularly if it is considered that there could be one, two or three providers, with different combinations of ALMO, CoCo and stock transfer.

Work within the project has taken place on an iterative basis to identify possible combinations which stakeholders might consider to be feasible in terms of cultural and management 'fit' – this has helped us present to stakeholders and the Steering Group possible combinations for consideration and feedback.

The outcome of this iterative process has been to focus on a series of combinations which have then been subject to wide ranging consultation.

3 Core assumptions utilised in our financial analyses

3.1 Introduction

In order to ensure that the financial comparisons between the options are equitable and allow stakeholders to make objective judgements around the financial implications, we have stressed made the same basic assumptions about rents, income and spending needs to underpin all financial analyses. This is critical so that there is not seen to be any bias or 'direction' identified towards the options.

The base financial year is 2011.12 and all options are modelled with this year as the starting point. The HRA for 2011.12 shows an in-year balanced budget after making provision for £4.66m of revenue contributions to capital, and financing for the HRA capital programme totals £32.59m. These budgets are subject to actual activity during the year and the council is reporting against these budgets on an ongoing basis. The core assumptions are therefore based on the approved budgets for 2011.12 and are set out below.

3.2 Property assumptions

Property numbers were 18,723 on 1st April 2011 split between providers as in table 1.

Table 1: analysis of stock by provider (1/4/11)

East Durham	8,436
Dale & Valley	4,262
Durham City	6,025
Total	**18,723**

Property movements included in the base plan are:

- 142 demolitions across the first 3 years
- 25 Right to Buy sales per year from year 2014 onwards (lower before).

3.3 Income assumptions

Rents are assumed to converge with rent restructuring formulae across the stock in line with government expectations in the self financing settlement by 2015.16. The split between provider areas is shown in table 2 below.

Average actual rents are reasonably close to average target rents (certainly compared to other local authorities) and we have therefore not assumed any delay to convergence as a result of the operation of the £2 annual limit on convergence. It is possible that some properties might not achieve convergence on time but these are felt to be immaterial in the overall plan.

Table 2: rents by provider area 2011.12

Provider area	2011.12 average actual rent	2011.12 average target rent
East Durham	£57.74	£58.80
Dale & Valley	£60.03	£61.58
Durham City	£61.21	£63.70
Stock average	**£59.38**	**£61.01**

Target rents are assumed to increase by RPI+0.5% in line with national government policy and the assumptions in the self financing settlement. Core inflation is 2.5% annually beyond 2012 (see below).

Void rates are averaged across the stock at 1.82% for all years.

Provision for bad debt totals £250k split between the providers according to stock sizes and averages 0.43% of the rent debit in all years of the plan.

Service charge income totalling £1.9m is assumed to increase with inflation with no further de-pooling included.

Other income covers non-dwelling rents and small budgets related to miscellaneous charges. These are also assumed to increase with general inflation.

3.4 Revenue expenditure assumptions

Management and maintenance costs are included at the level of 2011.12 budgets totalling £32.47m gross of any income - as set out below - and are assumed to move with general inflation.

Table 3: Gross service revenue costs by provider 2011.12 (£'000's)

Provider area	**ALMO fee**	**In house fee**	**Central costs**	**Special services**	**Manage ment**	**Repairs**	**Total**
East Durham	8,541		148	428	**9,117**	**5,384**	**14,501**
Dale & Valley	3,546		30		**3,576**	**2,830**	**6,406**
Durham City		2,862		638	**3,500**	**4,052**	**7,552**
Council (client)			4,282		**4,282**		**4,282**
Total	**12,087**	**2,862**	**4,460**	**1,066**	**20,475**	**12,266**	**32,471**

In line with the assumptions approved by the council in the Medium Term Financial Strategy (MTFS) from 2011-2016, the 2012.13 and 2013.14 financial years (years 2 and 3 of the modelling developed for this project) provide for efficiencies to be delivered from the management and maintenance budgets within the HRA.

The efficiencies included in the MTFS and which are therefore included in all of the modelling underlying all the options total £1.5m in 2012.13 and £3.0m in 2013.14. Further detail below these overall totals had not been developed or allocated during the period when the financial models were developed to report to the Steering Group. However, we would expect the council to be actively engaged in developing specific approaches to the delivery of efficiencies to meet the requirements of the MTFS in the preparation of the 2012.13 HRA budget.

We have developed the analysis of the above costs further below.

3.5 Capital profile assumptions

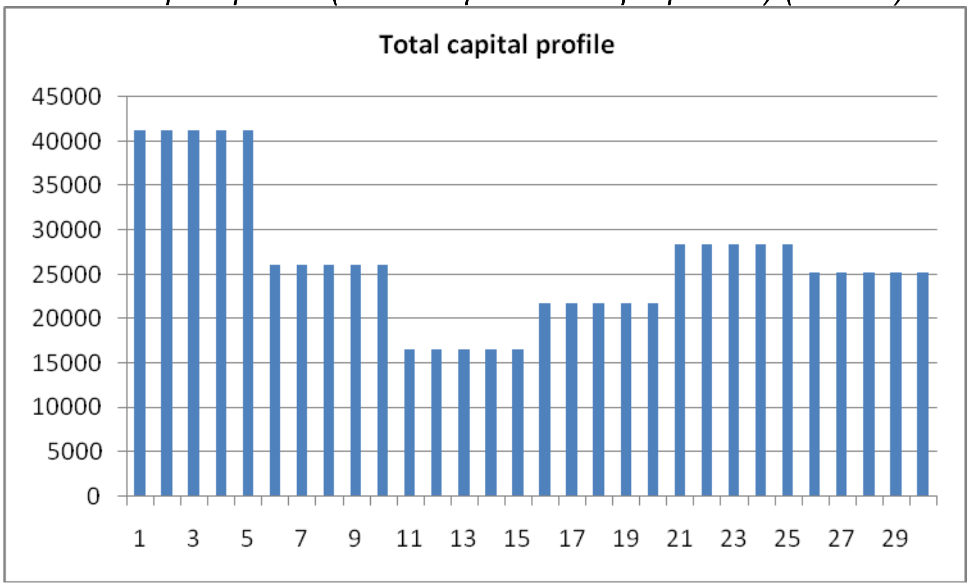
The profiles for capital expenditure are based on the databases held by each of the providers and a validation survey undertaken by Savills during 2010 and early 2011. Savills have indicated that the totals are consistent with the condition and nature of the stock and that they provide a sound and appropriate basis for the analysis of stock options.

Previous iterations of stock survey profiles indicated that meeting the total aspirations of tenants and residents and delivering significant regeneration to areas of stock in need of substantial investment might total upwards of £900m (at 2011.12 prices and post-demolition stock levels) over 30 years.

The validated outputs represent a modern maintenance standard for social housing and include basic decent homes works and life cycle replacements in line with industry standards. The profile might therefore be said to be modern but not aspirational.

The total investment need is £797m over 30 years which represents an average of c£40,000 per property over that period. The phasing of the investment needs are shown in the chart below.

Chart 4: Capital profile (2011.12 prices and properties) (£'000's)



The chart highlights visually the relatively 'up front' nature of the profile, with £337m (or 42%) focused into the first 10 years with a substantial backlog in the first 5 years.

Within these overall totals, the provider splits suggest that the spending needs are focused into the East Durham area in the first 5 years and the Durham City area in the following 5 years.

Overall, however, total average needs of the stock, after backlogs are met, over 30 years are quite consistent: £37,000/unit at East Durham and Dale & Valley, £35,000 at Durham City.

The decent homes backlog funding allocated to the council is £70m, received as supported borrowing approval in 2011.12 and capital grant from 2012 to 2015. In order to achieve a smoothing of programmes, we have assumed that the final year allocation of £26.3m is received (allocated) across two years (2014-2016).

There are two specific points about this allocation in the context of this report:

- The amount is some £37m lower than the outstanding former ALMO decent homes funding allocation relating to East Durham – programmes have therefore had to be scaled back as a result.
- It is assumed that this allocation is available to all the options (including stock transfer and CoCo options) – this is because decent homes allocations nationally have been made on the basis of the needs of stock and not whether the stock is owned/managed by local authority, ALMO or stock transfer housing association.

3.6 Economic assumptions

Where relevant, inflation, interest rate and discount factors vary between the options and we have set out in detail below how and why these variations arise.

However, as a core assumption, we have assumed that RPI inflation to April 2012 is 3.5% as this is consistent with the indicative settlement for self financing issued in February 2011 (see below), and 2.5% annually thereafter. This assumption might be seen as prudent given two factors:

- Actual expenditure costs are running a little lower than this in the forthcoming period given pressures on pay inflation
- Rents outweigh costs so a prudent assumption around inflation is advised so as not to overstate the net rental income arising in future years.

4 Developing the baseline financial analysis for self financing

4.1 National position and progress

The government published its main policy document in support of the implementation of self financing on 1st February 2011. Contained within this documentation was a model giving an indicative financial settlement for Durham's HRA along with supporting modelling identifying the assumptions that were utilised. Subsequent to the publication of this model, the government wrote to the council to indicate that it had found an error in its calculations and it had revised the indicative settlement for Durham.

In summary, the implementation of self financing for Durham on an indicative basis and therefore utilised throughout the modelling for this project, is based a settlement of £216m representing the present value of future guideline rents less an assumption of future expenditure allowances (management, maintenance and major repairs) discounted at 6.5%.

A settlement at this level would mean the council paying government c£15m on 28th March 2012, thereby released from paying negative subsidy payments in the future.

Preparations at the national level are now advanced with detailed timetables for the administration of the transaction in place and technical determinations towards debt charging, depreciation and other complex financial issues well in hand. Royal Assent for the Localism Bill is expected in late November and the government is expected to consult on final settlements in mid November with final figures set in stone mid-late January 2012.

The debt settlement is the product of a series of assumptions which are being made at the national level and, when published, the final draft settlement is likely to vary from the indicative settlement of £216m.

The main factors are:

- Increase in inflation which inputs to the starting rents for 2012 – the relevant September RPI figure was published recently and is 5.6%. This compares to 3.5% assumed in the indicative settlement – the impact might be to increase the debt settlement by anything up to £18m; this might result in a revised settlement of £234m albeit with higher input rents at the front end of the plan.

- Authorities have been asked to present summaries of planned demolitions and disposals so that these can be taken into account in reducing settlement payments. We understand Durham has included proposals for 140+ demolitions which should reduce the debt settlement marginally.

- All the usual factors affecting a subsidy settlement are being re-run for a final time to inform the settlement – it is difficult to predict how this might affect Durham given the inter-dependencies between all authorities with stock.

Taken together, we might expect the final draft settlement to be in the region of £230-235m but, notwithstanding the need for large rent increases implied by the RPI figure for April 2012, with no adverse financial impact on the business plan prospects set out in this report.

The final settlement is significant for Durham both in the context of the cost of the debt but in particular in the government setting a cap on debt at the level of the settlement. There is limited headroom below the cap to borrow post-settlement (as a result of the differences between current debt and the subsidy measurement of debt – HRA Capital Financing Requirement is lower than the Subsidy Capital Financing Requirement) of £15m.

4.2 Baseline self financing – additional assumptions

We have estimated the potential future cost of HRA debt by making an assessment of possible future interest rates. CIPFA has produced guidance which recommends the splitting of debt between the HRA and the General Fund (currently these are all pooled together).

The possible split of debt has implications for the HRA. Currently the HRA benefits from the council having pulled back investment in lieu of actual borrowing and is charged a lower consolidated rate of interest than is achievable through external borrowing. If the council opts to split the loans pools, this is likely to lead to a higher interest rate payable within the HRA on day one – we have assumed 5.37% (compared to less than 4% currently). This is in line with the guidance that CIPFA has published.

Although the government has announced a special one-off low interest rate through Public Works Loan Board (PWLB) borrowing for the settlement, as Durham's payment is relatively low compared to existing debt, the benefits to the council will be marginal.

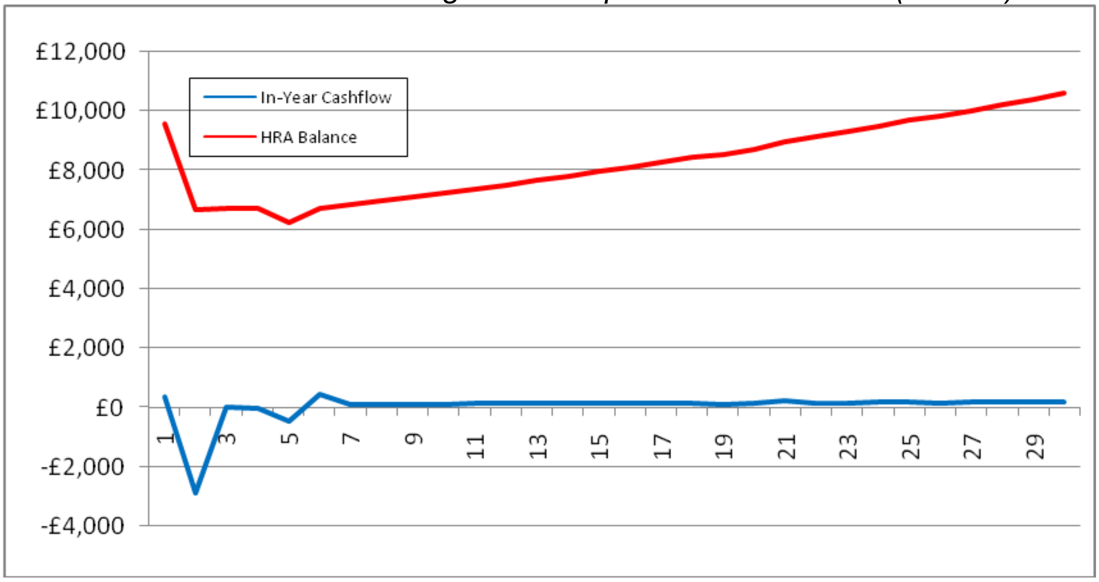
We have therefore assumed that interest rates reach a stable 6% from year 5 and stay at that level in the long term. Whilst it is likely that the council could outperform these rates, there remains less room for manoeuvre than in many other authorities.

4.3 Baseline self financing – outputs

Charts 5a, 5b and 5c show the baseline self financing business plan – the 'as is' situation continuing current policies – for revenue reserves, capital and debt.

Chart 5a shows that revenue balances can be maintained at or above the minimum level set throughout the 30 years but that no additional revenue surpluses are generated over and above the minimum.

Chart 5a: Baseline self financing business plan – HRA reserve (£'000's)



In comparing resources for capital which are available in each year with capital spending needs in each year, chart 5b shows that there is a shortfall of resources in each of the first 10 years followed by a period in which annual resources exceed spending needs. By year 19/20, the resources generated within the plan have 'caught up' with cumulative spending needs.

Chart 5b: Baseline self financing business plan – capital (£'000's)

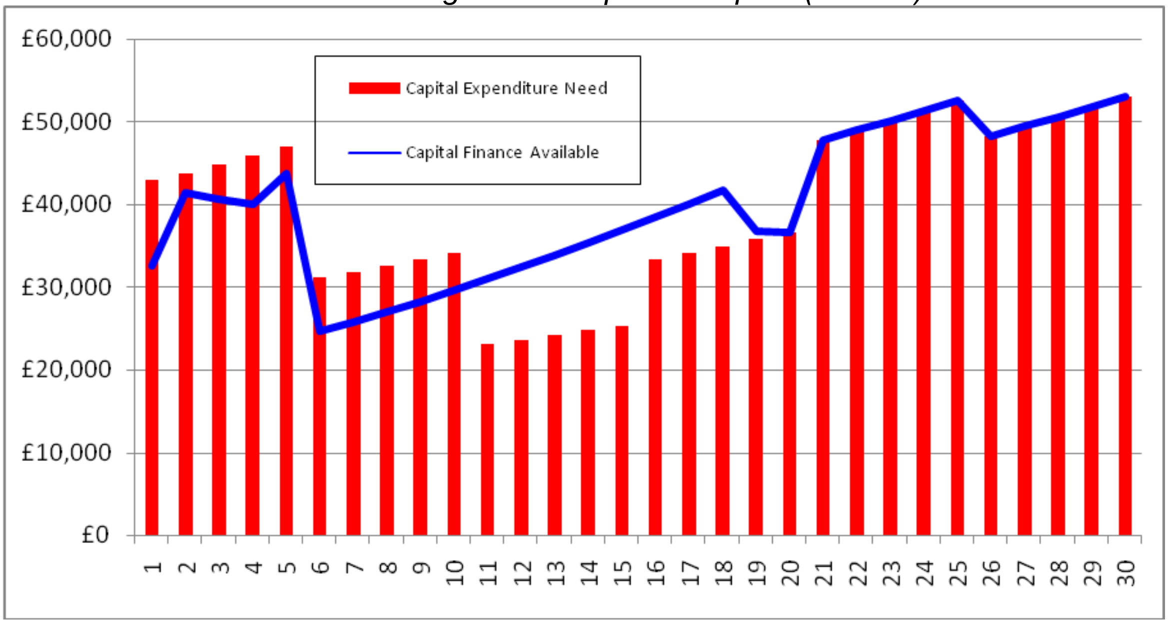
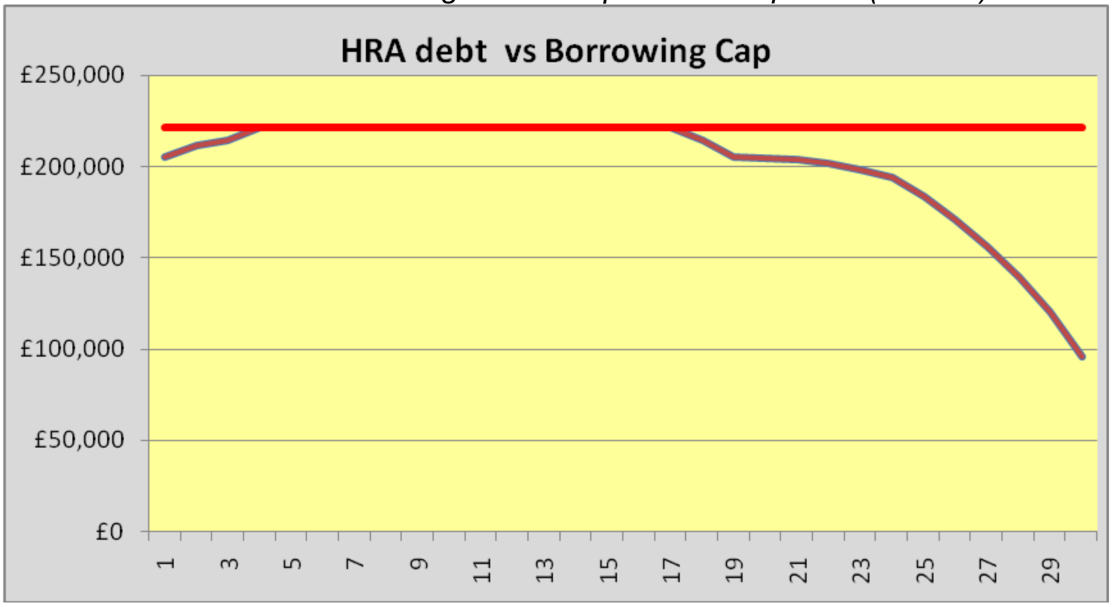


Chart 5c shows that additional borrowing is required to try to meet capital needs but that the cap is reached in year 4. Debt remains at cap until year 19 when surplus resources then allow debt to be reduced.

Chart 5c: Baseline self financing business plan – debt profile (£'000's)



The key conclusions from the above charts are set out below.

1. Capital spending needs are £388m for the first 10 years. Capital resources total £333m over the same period highlighting a shortfall of resources of £55m. After adding the effects of inflation, the shortfall rises to £63m over 10 years, or 16% of spending needs.

2. The operation of the debt cap is therefore significant for Durham; whilst in principle, it might be possible to construct a plan which borrowed further to achieve the investment needed, with efficiencies generated down the line to pay for the increased borrowing, such a strategy is prevented by the imposition of the debt cap.

3. If no additional resources became available to support capital spending in the first 10 years, around £63m of needs would need to be deferred – over an extended period of up to a further 9-10 years. Put another way, some works which are required now might wait up to 19 years until they are carried out.

4. The implications of deferring this level of investment for so long are exacerbated by the fact that some works have already been deferred from the first 10 years to reflect the reduction in decent homes funding.

5. If works can be deferred, the plan overall generates sufficient income to cover revenue and capital needs over 30 years. However the debt outstanding at the end of the plan period is c£100m. This indicates that the plan is unsustainable given the baseline assumptions – akin to borrowing money knowing that it was unable to be repaid.

6. In addressing the shortfalls in the baseline plan, further efficiencies would be required on top of the £3m included from the MTFS and/or additional resources generated.

It should be noted that the self financing settlement allows the council to generate and retain considerably more resources than if the HRA were to remain in the current HRA subsidy system. The resources generated by HRA business plans around the country are generally sufficient to maintain services and the stock based on a day-one position in which all backlogs have been cleared and all homes are at a decent and modern standard.

The specific issues affecting the viability for Durham arise therefore as a result of previous under-funding of capital investment in the stock; this means that there are outstanding backlogs of investment which the plan is unable to generate sufficient resources to address in the early period.

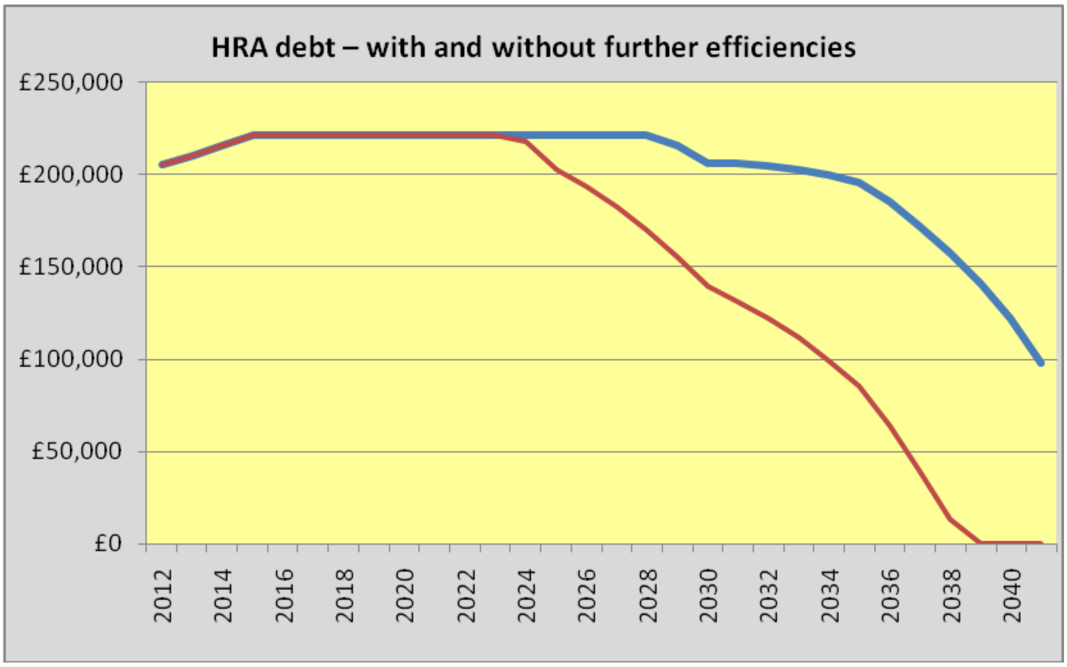
4.4 Baseline self financing – what would be required to balance the plan

In principle, strategies for addressing the shortfalls could be developed around revenue and capital cost savings and/or reductions in spending needs. Within the self financing regime, there could also be options to generate receipts through demolition and/or disposal.

Put simply, in order to balance the plan over the first 10 years, this would require £6m of savings annually (additional to the £3m annual efficiencies already built in). On a service cost base of £27m, this would represent one third of the service and is clearly untenable.

In order to balance the plan to zero debt at the end of year 30, this would require additional annual savings of up to £2.0m. The cumulative need for efficiencies would therefore be in the region of £5m pa against current revenue spending of £30m. If this were able to be delivered, the debt profile would be as shown in chart 6 below.

Chart 6: Baseline self financing business plan debt profiles (£'000's) with and without further £2m annual efficiencies



The chart highlights how the plan remains constrained by the debt cap for the first 10 years even moving along the bottom debt profile with additional efficiencies.

Capital shortfalls remain - £43m for the first 10 years. In effect, the delivery of long term annual efficiencies allows the plan to cover all costs over 30 years including debt, but does not address the need to generate additional resources for capital in the first 10 years.

Alternative approaches might include reducing capital profiles through active asset management – work by Savills is proceeding to investigate options and opportunities.

4.5 Analysing the business plan into provider areas

During the course of this project, we have been asked to comment on the possible financial position of the three provider areas on the basis that the plan might be capable of being analysed into three component parts. Such an investigation might have merit if, for example, it could be established that one (or more) of the provider areas were the main driver behind the challenges faced within the plan. Put another way, if the shortfalls arising in the plan are in one area only and a separate solution found for that area, the other two could remain with the council.

The spending needs and income are already split down between the three provider areas in the baseline plan. Testing the implications of 'three sub-plans' really therefore focuses attention on the main variable, which is the debt settlement. In other words, can we split the £216m debt settlement reliably between the three provider areas?

However, it is difficult given the passage of time to tease out what would be the differential position of each of the areas, particularly since we do not have data broken down into the three former district areas on any reliable basis since 2009.

We have identified three possible approaches to the splitting of the debt and then run separate provider-based business plans against these debt estimates. As would be expected, there is the potential for a wide variety of outputs – all of which are entirely dependent on the allocation of debt between the three areas. Possible debt split outputs are shown in the table below.

Table 7: Possible debt splits between provider areas (£m)

Basis	East Durham	Dale & Valley	Durham City	Overall
A-Current debt pro-rata	100.2	86.3	29.8	**216.3**
B-Per unit pro-rata	97.5	49.2	69.6	**216.3**
C-Estimate from 2009 subsidy allowances	71.8	51.7	92.8	**216.3**

Under scenario A, the debt would be split per the legacy debt from the previous component district HRAs. Both the East Durham and Dale & Valley business plans would be unviable with the Durham City plan generating considerable additional resources.

Similarly, splitting debt on a simply per unit basis (scenario B) leads to an unviable plan for East Durham with a highly resource rich plan for Durham City; Dale & Valley might be made to work with additional efficiencies at this level of debt. The variation between outputs is founded on the nature of the stock, rents and costs between the three areas – these would not be reflects if the split was on a simple per unit basis.

If we estimate the allowances for management, maintenance and major repairs rolled forward from 2009 (the last year in which separate subsidy settlements for the three former districts were received) and plugged these into the national settlement model, this would suggest a highly variable debt/unit for each of the areas, ranging from £8,500/unit settlement for East Durham, through £12,100/unit for Dale & Valley, to £15.400/unit for Durham City. In theory, this type of split might reflect the nature of the stock and the former authorities.

In practice, placing these debt settlements into constituent business plans suggest that each would have similar difficulties and challenges. For East Durham, the challenges remain with shortfalls in the first 5 years. For Dale & Valley and Durham City, the challenges tend to be in the year 6-10 period. The cost bases of each plan would be closer to the allowance distribution represented in the different settlement amounts – this however leads to all three sub-plans demonstrating difficulty in covering debt fully over 30 years. Put another way, the requirement for efficiencies remains spread across all three areas.

The above highlights that the debt can be split on a range of bases with very extreme positive or adverse consequences at the area (or sub-plan) level. In effect, the council could split the debt however it wanted if it felt this would be an appropriate method of delivering the self financing plan in the future.

The central conclusion is therefore that any individual area or combination of areas might be deemed to have the greatest financial challenges – all is dependent on the debt that is allocated.

For the stock transfer options, the approach that the government might take to debt allocation should an individual provider area be the subject of a specific and separate transfer proposal, might need to be based on some assessment of the rents and allowances in the area concerned – this is addressed below. However, our sense is that the government would only be able to apply alternative methodologies as above in order to arrive at an equitable approach.

4.6 Summary: baseline self financing business plan

In summary, the self financing business plan highlights shortfalls of capital resources against spending needs of £63m over 10 years, which is 16% of total needs in that period. Whilst the plan can generate sufficient resources to meet needs over 20 years, the council might consider that the deferral of this amount of investment over such an extended period is untenable.

£100m of debt would be outstanding after 30 years which would need to be addressed if the plan is to demonstrate long term viability – this suggests a need for a further £2m savings over and above the £3m annual efficiencies included in the baseline plan.

The central issue is therefore that the operation of the debt cap under self financing is incompatible with the up front nature of the investment needs. A solution is therefore needed which enables the council and providers to achieve the full investment profile in all years.

An analysis of the individual plans for each provider area shows that the viability of each would be completely dependent on the allocation of debt settlement between three sub-plans. There are such wide potential variations in the allocation of debt between areas that the analysis feels rather an academic exercise. As time moves on, it is less likely that the formulae bases for the former subsidy allowances will continue to apply robustly to the stock in each area.

5 Overview of provider costs

5.1 Introduction

Work has been undertaken to review the overall costs of services within the three provider areas and to test the potential for efficiencies to be delivered in support and back office services within the three providers. Comparisons of unit costs against 'expected' costs (however established) might prove a basis for targeting efficiencies should a sufficiently robust methodology be capable of being developed for determining a view of 'expected' costs.

As part of the next stage of work on the appraisal, the council may wish to explore in more detail the feasibility of options to merge the governance and management structures of two or more of the providers. At this stage, however, the work undertaken in the project has focused on a high level analysis of overheads and support costs. No work has been undertaken to test options or opportunities to seek efficiencies or cost savings in front line services; providers have been asked to propose their own efficiencies as part of the 2012.13 budget process.

5.2 Provider costs in the baseline plan

The table below shows the gross management and maintenance costs included in the baseline plan, reduced for non-rent income and also on a per unit basis. Net management and repairs costs are, for example, £1,500 per unit in East Durham in the 2011.12 budget, including management fee and an allocation of some directly recharged costs. Central costs represent £229/unit overall for the whole stock.

Table 8: Analysis of service revenue costs against prior subsidy allocations

Provider area	M&M gross £'000's	Income £'000's	Net M&M £'000's	Per unit £	MMA 09 *
East Durham	14,501	-1,851	12,650	1,500	1,640
Dale & Valley	6,406	-644	5,762	1,352	1,555
Durham City	7,552	-220	7,332	1,217	1,410
Council (client)	4,282	0	4,282	229	-
Total	**32,741**	**-2,715**	**30,026**	**1,604**	**4,605**

** Management and maintenance allowances in the last year of separate subsidy*

Despite the apparent wide variation in unit costs between the provider areas, there is consistency in cost bases against what was, for many years, the basis of resources for revenue services (ie management and maintenance allowances in the HRA subsidy system).

The position is affected by a central cost representing £229 per property. If this is allocated evenly across provider areas, the East Durham area might be highlighted as higher cost when compared to former allowances. However, there might be many ways to allocate these central costs, for example the Durham City area might be held to consume more services given that it is an in-house service.

This high level analysis shows that there are many different ways to draw potential conclusions around the unit costs between providers and between them and the council. This might therefore suggest further development of the analysis aimed at targeting efficiencies more effectively between providers. In the context of the overall appraisal, the inclusion of £3m from 2013 and the potential need for further savings to balance the self financing plan (in the absence of other options or resources), might obviate the need to establish a formula based approach.

5.3 Support service costs

A short piece of work was undertaken with the finance officers from the three providers to identify the total costs of management, support and back office services.

Using the budgets set within the HRA and within the ALMO accounts (financed by management fee), an analysis of the total costs of specific groups of services was developed. The exercise resulted in the high level summary outputs below and highlighted the following key issues:

- There is a variety of experiences of support, management and central cost structures between the three providers, with East Durham Homes having a full infrastructure, Dale & Valley Homes partially sharing services with the council and the council supporting both Durham City Homes as well as the central costs within the HRA.

- From an external perspective, we were struck by the extent to which service sharing was already taking place (eg for income collection and cashiers).

- Notwithstanding the differential experiences, the total of support costs is not insignificant and appears to offer some potential for further detailed exploration of opportunities to meet the efficiency targets in the MTFS.

Table 9: Summary of support and central budgets 2011.12 (£'000's)

Area	Budget 2011.12
Management	1,164
Finance	686
Legal	196
HR	278
IT	1,017
Audit	291
Quality/Strategy	591
Governance	242
Accommodation	531
Support/communications	335
Total	**5,331**

The table highlights £5.3m of budgets for support services out of a gross management cost of c£17m and gross service revenue cost of £32m. This total therefore represents around 15% of total costs and 30% of management costs.

Whilst these might not appear to be on the high side for local authority housing services, the scale of the costs might suggest that there is scope for efficiencies through rationalisation.

In addition, there is a budget in the HRA of £1.1m for corporate and democratic core costs. Although a breakdown of these is hard to develop given the huge undertaking that is Durham County Council, this tranche of costs might also usefully be subject to further analysis in order to seek efficiencies.

We understand that finance officers within the providers are taking forward the analysis of support with council officers with a view to identifying the scope for rationalisation moving forward.

6 Alternative options: traditional large scale voluntary transfer (LSVT)

6.1 Introduction to the option

Stock transfer to a housing association has proved to be a highly successful mechanism to lever in additional private finance to council housing stock over a period of 20+ years. Just over half of all authorities have transferred their housing stock since 1988, raising over £20billion of private finance over that period.

The financial landscape for LSVT has however changed radically in the recent past and will be changed fundamentally and irreversibly with the implementation of HRA self financing.

The background to transfer is familiar to stakeholders within Durham and we have not sought to repeat often reported facts around the option in this report; we have focused on the financial factors and implications only, specifically also in the context of options for the housing stock and the HRA.

We have not sought at this stage to identify any differential financial implications of pursuing transfer to the existing providers or a newly created or existing housing association in partnership with the current providers. A preliminary seminar was held with county-based providers during September 2011 in which some expressed a desire to explore working with the county in more detail as the appraisal develops.

Stock transfers have taken place with significant incentives from public finance over many years. The assumptions utilised in valuation of the housing stock, the ability to get overhanging debt written off if the transfer price does not cover existing housing debt and a relatively generous treatment for future capital receipts have all incurred a public expenditure subsidy which was not available to those authorities retaining their stock. The stock transfer option has therefore developed an infrastructure and momentum in which the private finance markets are well established and finance has been relatively inexpensive.

The implementation of self financing has changed the bases of these assumptions at the same time as the government has sought to reduce the public subsidy for transfers in line with reductions in public expenditure across the economy.

In preparing for self financing, the government has explicitly stated that the starting assumptions for any future transfer would be the same as those utilised in the self financing settlement calculation, ie at expenditure levels which are the allowances included in the HRA settlement.

Assumptions for traditional stock transfer have focused on increased expenditure in order to incentivise the transfer and to provide reassurance to funders that sufficient resources would be available to maintain the stock and therefore service/repay their borrowing.

There is therefore a gap between the assumptions for self financing and what might be the expectations under a traditional stock transfer model. An analysis of this is set out below.

It should be noted that the government has signalled its intention to update its guidance on stock transfers in the autumn of 2011 and that there is a reference to the potential to negotiate around value for money in future stock transfers. In practical terms, this is likely to mean making a case around how transfer can increase value for money for the public purse by securing investment that might otherwise have to be deferred under self financing and therefore become more inefficient. On this basis, the council should therefore retain stock transfer as an option under consideration.

6.2 Key financial features and assumptions for LSVT in the self financing system

Notwithstanding the financial assumptions applied to transfer, the option remains open to the council for partial stock transfer, transfer of one or more provider areas or transfer of the whole stock.

The valuation of the housing stock would be based on the full stock capital profile and provide for VAT on all external capital and revenue works throughout the lifetime of the plan.

If transfer was to a charitable housing association, which could be the existing providers reconstituted as Registered Providers, a VAT shelter could be established to reclaim VAT on capital works for up to the first 15 years of the business plan.

Valuations of the housing stock are set out below and these would form the price paid by the acquiring housing association(s). The valuation becomes a receipt to the council. The receipt would be set against HRA debt. Since 2003, any overhanging debt has been able to be cleared by government – although this mechanism remains in place, it is highly likely that the arrangements and level for debt write off will be very tight post-self financing. Transfers which have proceeded during 2011 have seen a level of overhanging debt write-off at much reduced rates compared to those seen before 2010.

There are a series of other financial implications which are listed briefly for reference; these would need to be developed further if stock transfer became a preferred option, however at this stage, these factors are not central to the financial appraisal:

- The HRA would be closed upon whole stock transfer
- Support and central services currently provided by the council could continue for up to 12 months post transfer; costs currently charged into the HRA form the council's General Fund would fall on the General Fund and efficiencies required
- There would be sharing arrangements put in place for future capital receipts
- The VAT shelter would be subject to agreement around utilisation of the proceeds between the council and housing association(s).

6.3 LSVT valuations for Durham under the self financing system

The table below sets out the estimated valuation of the housing stock in each provider area if transfer was able to proceed on the basis of traditional assumptions ie meeting all the needs of the stock in the year that they arise in line with the full stock condition survey and current spending patterns for management and day to day repairs.

The outputs reflect the different levels of rents and management expenditure as well as the phasing of capital investment needs as set out above. The table highlights the base position and the position with the inclusion of decent homes backlog funding.

Table 10: LSVT valuations by provider area (£m)

Area	Base valuation	DH funding	Revised valuation
East Durham	-101.6	+70.0	-31.6
Dale & Valley	+3.7		+3.7
Durham City	+33.6		+33.6
Whole stock *	**-64.4**	**+70.0**	**+5.6**

** totals differ due to rounding*

The key bottom line financial valuation is therefore £5.6m for the whole stock, which takes account of the inclusion of decent homes backlog funding of £70m.

The overall valuation masks a wide range with a highly negative valuation in East Durham and a positive valuation for Durham City's stock. These variations in valuation are very dependent on the differing level of rents and management costs across the provider areas.

The experience of recent stock transfers has been that the government has been keen to reflect an increasing benefit from VAT shelters back into the business plan, in effect increasing the valuation sustainable by the stock. If it is assumed that a 15 year VAT shelter on capital works can be worked back into the business plan, table 11 shows the resulting revised valuations.

Table 11: LSVT valuations amended for VAT shelter add back (£m)

Area	Core LSVT valuation	With VAT shelter added back
East Durham	-31.6	-9.3
Dale & Valley	+3.7	+14.5
Durham City	+33.6	+50.7
Whole stock *	**+5.6**	**+55.9**

** totals differ due to rounding*

The valuation of the Durham council housing stock for stock transfer purposes, including VAT shelter and on the basis of 'traditional' assumptions, is c£56m.

6.4 Debt implications for LSVT in Durham

The valuation has implications for the treatment of debt housing debt in a self financing context.

Table 12 below shows the 'gap' between the reduction in debt that might be delivered through negotiation with government around VAT as an allowable expense and the valuation set out above.

A reduction in the HRA debt relating to the addition of 5% to management and maintenance allowances and 20% to the major repairs allowance in the indicative debt settlement represents out estimate of the debt adjustment that might be achieved on transfer – an estimated reduction of £66m leaving £150m of HRA debt to be cleared upon transfer.

Table 12: Overhanging debt gap under whole stock LSVT (£m)

Area		**Debt/valuation**
Self financing debt settlement		£216m
Reduction for VAT as an allowable expense		-£66m
Likely starting point for government negotiation on debt reduction		£150m
Value for money 'gap'		**£94m**
LSVT valuation with VAT shelter added back		£56m
Traditional LSVT valuation with backlog funding		£6m
Traditional LSVT valuation		- £64m

Put simply, whilst the government might reasonably be expected to reduce debt to £150m for stock transfer, the markets and funders might expect to finance a maximum valuation of £56m. The 'gap' is £94m.

The options for reducing this gap include:

- Contribution from the council (this might include land and other receipts or resources put in to assist financing the transfer).
- Contribution from purchasing housing association(s) – this might take the form of gift aid or up front investment, or paying a 'higher' price so as to generate additional value in the future.
- Further debt write down by the government, strictly on the basis of a value for money case around why a transfer can deliver investment that self financing could not.
- Relaxation of funding criteria by lenders so that funding is made available to a higher level than might previously have been the case – the price of such finance might therefore be higher.

These are generic options and do not represent anything other than a significant challenge in making a whole stock transfer work financially for Durham.

6.5 Partial transfer options

If the council were to pursue partial transfer options for each of the provider areas, the main factors arising are as follows:

For East Durham, as the stock is negatively valued overall, including the VAT shelter add back, there would be a need for additional overhanging debt support either from the government and/or a purchasing housing association. If the transfer was at nil price, the remaining HRA would benefit from the avoided cost of any negative value.

For Durham City and Dale & Valley, transfer could proceed on the basis of a positive valuation; however, the potential level of debt reduction would leave the remaining HRA (predominantly the current East Durham stock) in a worse position – ie the East Durham stock would need to support a higher debt than sustainable even within the baseline self financing model.

The council might also consider its options to pursue local transfers of specific areas or types of stock in order to improve prospects for the remainder of the HRA stock ad these might emerge from the work being undertaken by Savills.

6.6 Summary of LSVT options in Durham

The financial landscape for traditional LSVT has changed significantly and transfer can now only proceed on the basis that expenditure assumptions are in line with those made under self financing.

Taking into account the receipt of decent homes backlog funding and the potential to claim a VAT shelter for 15 years, a maximum transfer valuation for the whole stock would be c£56m.

This compares to a potential reduced debt position of £150m upon transfer leaving a gap of c£94m to be bridged.

Whilst funding towards this gap could be identified across the council, a purchasing housing association or by changing the basis upon which private finance is made available under LSVT, these sources are unlikely to bridge the whole gap. The council would need to mount an argument to government seeking additional debt write off on transfer based on a value for money and efficiency case around the timing and effectiveness of investment.

The government is due to update its transfer guidance in the autumn of 2011 which might set out the basis upon which it might consider such a case post-self financing.

At the provider level, a transfer for East Durham would require dowry funding. For Durham City and Dale & Valley, although positive, transfer of these two would leave the remaining HRA with too high a debt to sustain unless further debt write off from government could be secured.

7 Alternative options: Council/Community Company (CoCo)

7.1 Introduction to the option

In the spring of 2011, the National Federation of ALMOs (NFA) published a research report into the development of community-based and private finance models for ALMOs. The research was undertaken partly in response to the need to develop a future direction for the ALMO movement and partly in response to the implications of the implementation of the self financing system for private finance.

The research exemplified two potential private finance options for ALMOs going forward, both predicated on the transformation of an ALMO based on moving towards a different ownership model and delivering the ability to borrow for investment above the debt cap imposed under self financing:

1. A PFI-style long term management agreement in which the ALMO would be able to borrow against future management fee income

2. A stock transfer model, in which the HRA debt stays with the council to be serviced by the newly constituted ALMO and private finance can be levered in on the strength of the asset base; the term CoCo (based on the reconstitution of the ALMO as a Council/Community partnership) has entered popular parlance in order to describe this model – the description captures the ongoing partnership within the business plan with the council retaining a direct pecuniary interest in the delivery of the plan – and its contrast with a traditional stock transfer in which the direct financial interest of the council is removed.

Given that the challenges and issues within the early years of Durham's HRA baseline plan are linked to constraints imposed by the debt cap, the models merit review and appraisal in this project in order to test the ability to meet the capital spending needs when they arise.

The council and Steering Group, on our advice, have not considered in detail the potential to establish long term management contracts (see 1 above) – principally these are a subset of modelling the CoCo option. We have therefore set out below some of the key financial factors associated with a CoCo option in Durham.

It should be noted that this is as yet an undelivered model as it is dependent upon the implementation of self financing. The council and Steering Group should therefore see the analysis below in that context. At the time of writing, there are three other ALMO authorities that have expressed an interest in exploring the model in detail.

7.2 Key features of the CoCo model

The model would be based on changing ownership of an ALMO to one that has a minority interest by the council (49% or less) and governance along the established third:third:third model in common with stock transfers and ALMOs.

Details of the legal and organisational implications are included in a separate report from the council's legal advisers, Trowers and Hamlins.

Financially, the key features are as follows.

- Stock transfers to the ALMO/CoCo following a ballot of tenants.
- The transfer is at nil price based on the council retaining the HRA debt after transfer to be serviced by the ALMO/CoCo.
- Because the CoCo is subject to irrecoverable VAT and VAT is an 'allowable expense' in public expenditure terms, the HRA debt would need to be reduced on transfer to reflect the element of VAT on expenditure allowances in the self financing settlement calculation.
- Conversely, if the ALMO/CoCo becomes charitable, it should be possible to negotiate a VAT shelter with HMRC – this would allow the recovery of VAT on capital works for up to 15 years.
- The ALMO/CoCo would service the council's outstanding debt up to the borrowing cap and would be able to borrow additional finance above the cap from private funders.
- The cost of private finance would be higher than could be obtained via the HRA/public sector – within the NFA research, the estimate was an additional 1.3% interest rate on debt above the cap. Future rental income can then be committed to pay down the private finance along traditional lines – ie within 30 years.
- Discussions between the NFA and funding advisers have suggested that security for the borrowing could be split between the council (for the HRA debt) and the funders (for the private finance).

The advantages of the CoCo model over a traditional transfer include a continued financial interest by the council and access to continued cheaper finance via the HRA debt.

7.3 Application of the CoCo model to Durham

We have developed an analysis which models the CoCo option for the whole stock in Durham. Compared to the baseline self financing plan, the following assumptions are changed:

- A reduction in the HRA debt relating to the addition of 5% to management and maintenance allowances and 20% to the major repairs allowance in the indicative debt settlement. This results in a reduction of £66m and an opening debt of £150m. It is important to recognise that, whilst government have acknowledged that this would be an allowable reduction, as for the LSVT option, the actual amount would depend on negotiation.
- The addition of 20% VAT to capital works from years 16-30.

- The addition of 5% VAT on management and 8% on revenue repairs costs, representing VAT on external/supplier costs within overall revenue budgets.
- The inclusion of £3m set up costs.
- Addition of 1.3% to the interest rates in the baseline plan, applying to borrowing above the debt cap (7.3% over the long term).

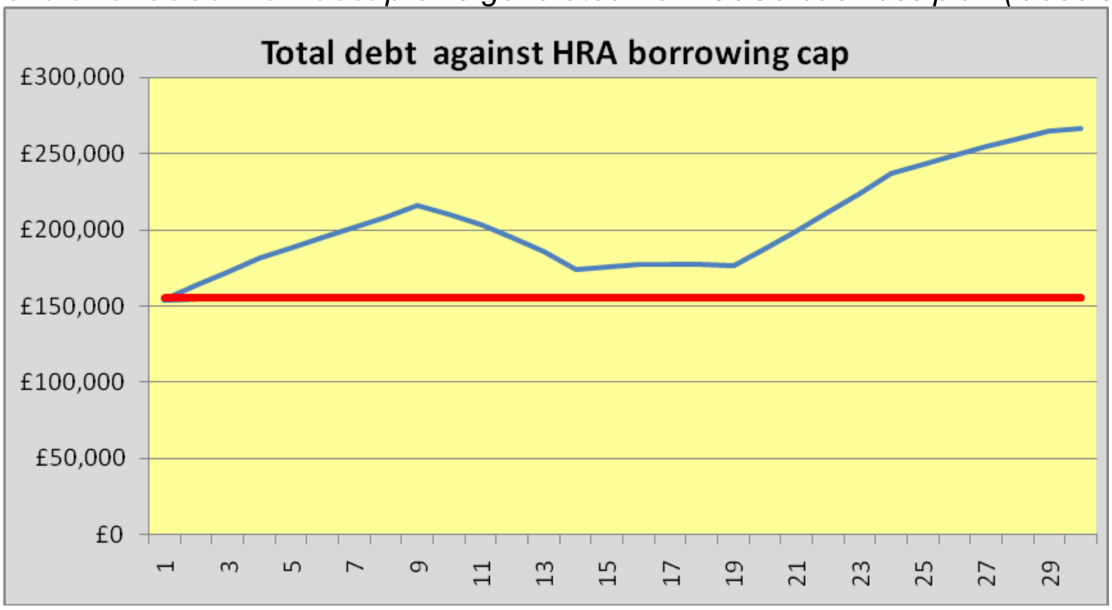
All other assumptions as included in the baseline plan are unchanged – with the fundamental principle included that borrowing above the cap is drawn down to meet capital spending needs in the year that they arise.

7.4 CoCo model outputs for Durham

The outputs from the CoCo model at the whole stock level are therefore in the form of a debt profile arising as a result of meeting all spending needs.

The raw profile generated from the assumptions set out is shown in chart 13 below.

Chart 13: CoCo - raw debt profile generated from CoCo business plan (£'000's)



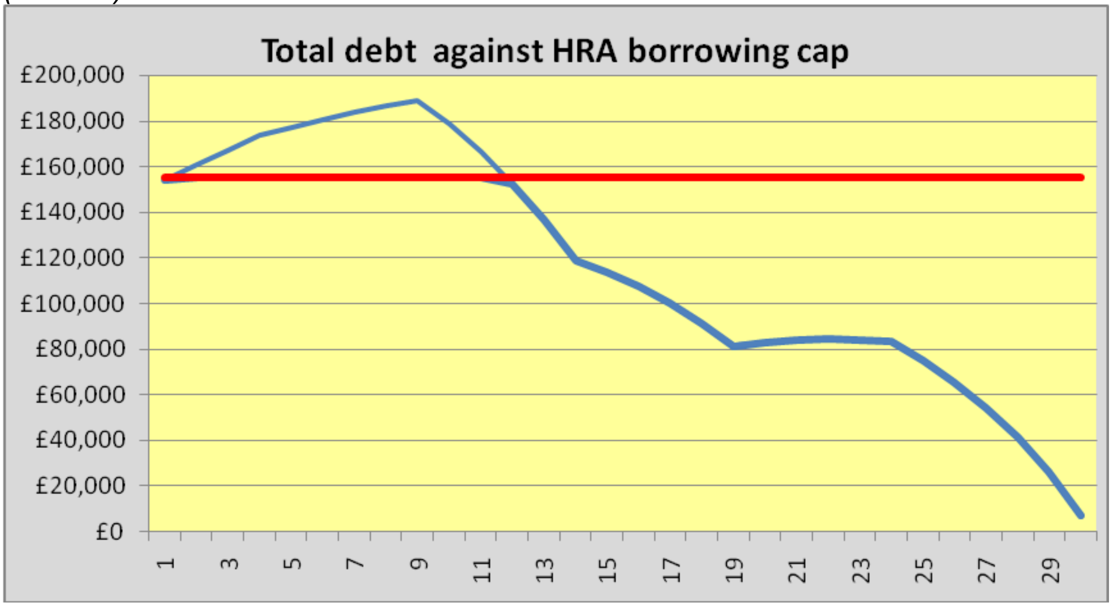
The chart shows that the model would not be viable without efficiencies to deliver sufficient surpluses to cover debt – particularly after year 16 when VAT on capital works becomes a net cost to the business plan. Debt is rising after 30 years.

Such a model could therefore only work with additional of efficiencies. Two approaches might be adopted:

- Deliver additional efficiencies in all years of the business plan – this would require the equivalent of £2.25m of savings in all years of the plan.
- Deliver efficiencies when required from year 16 – this would require the equivalent of over £5m per year for the latter half of the plan.

As it would be unlikely that private finance could be obtained on the basis of a promise of future efficiencies in 16 years time, the former approach might seem more appropriate. If applied, chart 14 shows the resulting debt profile.

Chart 14: CoCo – amended debt profile with £2.25m additional efficiencies (£'000's)



The analysis of the CoCo option therefore highlights the need for additional efficiencies in order to achieve the level of viability within the plan that funders and the council would require.

From a financial perspective, a positive output is the relatively low level of additional borrowing required in the early years to achieve capital needs and address backlogs – less than £50m overall – and the relatively short time period required to repay the private finance above the cap. Greater flexibility to level in future investment would therefore be possible under this model.

The identification of a requirement for additional efficiencies is similar to the findings for the self financing baseline model – it is therefore likely that additional efficiencies will be required under any model in which HRA debt remains in place.

7.5 CoCo model for individual providers

On an illustrative basis, we developed a model to test the CoCo option for each of the provider areas individually. Rather as for the findings on individual self financing plans, the viability is entirely dependent on the allocation of debt between the three areas.

Building on the analysis of debt allocations (above) based on former district authority allowances, a speculative estimate of debt reductions would suggest figures in the region of £21m for Durham City, £30m for East Durham and £15m for Dale & Valley.

These estimates must be treated with caution given the multiple assumptions and caveats applying. However, if applied to the individual plans in a CoCo context, the main findings are that, as for illustrative individual self financing plans, the requirement for additional efficiencies applies across all three plans.

It would not be possible therefore to identify one or more or the provider areas specifically as appropriate for a CoCo model, although as the shortfalls in the very early years apply mainly in the East Durham area, this might suggest that the model could apply with greater merit than in the other two areas.

Clearly, if the council were to pursue an overall approach in which one or two provider areas moved towards a CoCo model, the council would aim to increase the amount of debt reduction on transfer so as to ensure greater viability for the CoCo business plans. The aim would be to ensure that an individual provider CoCo was viable along with any ALMO model that continued to manage an element of retained housing stock.

7.6 Summary of CoCo model for Durham

The Council/Community (CoCo) company model might have merit in Durham given that the financial pressures in the business plan are in part caused by the constraints of the HRA borrowing cap.

The CoCo model could allow private finance borrowing to meet needs above the cap which could then be repaid during the lifetime of the business plan. At the whole stock level, this could total less than £50m on the basis of a £66m reduction in HRA debt on transfer to the CoCo. The debt reduction would be subject to negotiation with government but indications are that such a reduction would be achievable.

As with the self financing plan, however, additional year on year efficiencies over and above those included in the current MTFS would be required in order to achieve viability.

At the provider level and from a purely financial perspective, the CoCo model might in principle apply most usefully in the East Durham context where spending pressures are the greatest in the early years. Pursuing a CoCo model for East Durham might suggest a reduction in HRA debt of c£30m although this would be subject to negotiation with government.

8 Option combinations

During the course of this project, we have been asked to advise on the possible combination of options for each of the provider areas and for the whole stock that might be deliverable. The table below summarises the various potential combinations that were presented to the Steering Group jury session on 24th June and is included in this report as a record of the course of the debate.

Since that date, the Jury and stakeholders have narrowed the options for wider consultation and reports from the council's officers set these out in more detail.

Table 14: option combinations presented to the Steering Group

	EDH	DCH	DVH	Comments
1	*ALMO*	*In house*	*ALMO*	*Capital shortfall – need additional efficiencies (£2m)*
2	In House			Capital shortfall – need additional efficiencies (£2m)
3	ALMO (three delivery arms)			Capital shortfall – need additional efficiencies (£2m)
4	ALMOs with shared support			Capital shortfall – additional efficiencies found from support… £2m needed
5	CoCo	CoCo		Debt write down £66m - £2m efficiencies needed – could be a Group (synergy)
6	CoCo	ALMO		Debt write down £48m - £1m efficiencies CoCo/£1-2m HRA
7	ALMO	LSVT	ALMO	Debt write down £13m – receipt £50m – efficiencies £2m – debt o/s yr30
8	CoCo	LSVT	CoCo	Debt write down £66m – receipt £50m - £2m efficiencies needed in CoCo's
9	CoCo	LSVT	LSVT	Debt write down £66m – receipt £64m - £2m efficiencies needed in CoCo
10	CoCo	LSVT		Debt write down £66m – receipt £64m - £2m efficiencies needed in CoCo