DERBY CITY COUNCIL

COMMUNITY COMMISSION
14 January 2008

ITEM 8A2

Report of the Corporate Director – Corporate and Adult Services

HRA Business Plan and Budget 2008/09 - Consultation

RECOMMENDATION

1. To ask for the Commission's views on the consultation document on the Housing Revenue Account, HRA, Business Plan and Budget 2008/09, attached at Appendix 2.

REASONS FOR RECOMMENDATION

2. The Council consults with Derby Homes, tenants, and the Community Commission on its HRA budget plan update each year.

SUPPORTING INFORMATION

3.1 The consultation document sets out in detail the position facing the HRA in the next year and for a thirty year forecast period. The overriding policy remains to use the additional funding that the HRA has in the short term to achieve two strategic goals: stability in the HRA on the loss of additional funding in 2012 and the provision of the estates pride programme of £15m. The key issue is the extent to which the overall funding can be relied upon to achieve these goals, and the conclusion drawn is that whilst the plan is viable the assumptions made will need to be monitored closely as they are critical in the long term.

3.2 The consultation document makes it clear that the plans are contingent on maintaining the currently relatively low level of spending on maintenance into the future and also on obtaining a real terms increase – known as rebasing – as a result of real terms rental increases beyond the rent restructuring period. This is a longer term issue but affects the perception of how much funding can be spent now. As these are relatively optimistic scenarios, there could be a case for spreading out the spending of Estates Pride over a longer timeframe than currently allowed to allow for greater flexibility in the plan to respond to any deterioration in the position in the future.

3.3 The timetable for consultation is:

14 December onwards – Derby Homes Senior Management
14 December - HRA Strategic Working Party
14 December – City Housing Consultative Group
14 January – Community Commission
20 February – Cabinet meeting

3.4 It should be noted that the consultation document is drafted on the basis of the draft determination issued in November. The final determination is expected at some point during January. Should there be a material change to the figures, there may need to be changes made in the final report to Cabinet. This will be verbally reported on at the meeting.

OTHER OPTIONS CONSIDERED

4. Other options to the existing strategy could place the longer term future of the HRA's finances at increased risk if substantial additional expenditure was committed. Discussions are ongoing between the Council and Derby Homes about their management fee.

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Background papers:	Draft determination November 07
List of appendices:	Appendix 1 – Implications Appendix 2 – Consultation Document

IMPLICATIONS

Financial

1. Set out in the report.

Legal

2. The Council is required to set a budget for its Housing Revenue Account that balances and that charges costs appropriately to either the HRA or to the General Fund.

Personnel

3. None directly.

Equalities impact

4. Many of the Council's tenants belong to the Council's equality target groups.

Corporate objectives and priorities for change

5. The objectives of **strong and positive neighbourhoods, protecting and supporting people**, and a **healthy environment** are all enhanced by the improvements in council house standards as a result of Decent Homes, and by any improvements possible through the Estates Pride programme.

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Consultation Document

ITEM XX

Housing Revenue Account Business Plan and Budget 2008/09

Key Issues

1 The Housing Revenue Account, HRA, remains financially robust in the short term but faces some significant uncertainties going forward. The recent draft subsidy determinations have added to these uncertainties and as a result the current HRA business plan should be viewed cautiously.

2 The current position for the HRA has improved significantly to that reported last year the principal reasons being:

- Lower than anticipated capital financing charges
- Lower Leasing costs as a result of termination negotiations
- Increased HRA reserves on which interest is earned

The current year's projected outturn is anticipated to be underspent by around £0.2m, due mainly to the interest earned on higher than anticipated HRA balances.

3 The proposals allow for the continuation of the Estates Pride programme of works with a view to supporting a £15m total programme over a number of years. The Council has already committed £9.095m of this programme, and it is suggested that the Council authorise the drawing up of plans for a further £3m of Estates Pride funding which would take the total committed to £12.095m. The remaining balance of the Estates Pride programme will be reviewed each year in the light of the financial position as it is then.

4 The proposals also include additional funding of £285k to cover the replacement Housing Management system identified by Derby Homes together with a contingency of a further £100k to cover the possible costs of job evaluation.

5 This consultation document is based on the draft determination of housing subsidy for 2008/09 issued by the Department for Communities and Local Government, DCLG, in November 2007. The final determination will be issued in early January and, if materially different to the draft, may require changes to the final proposals made to Cabinet in February 2008.

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Consultation Document

Review of HRA financial position 2007/08

1 The aim of the Housing Revenue Account, HRA's, financial strategy remains to generate sufficient funding in the short term to allow a relatively smooth transition at the end of substantial additional ALMO funding in 2011/12 of over £2.5m a year. In addition, an Estates Pride fund of £15m for improvements to estates and facilities available for the benefit of tenants also needs to be supported.

2 This strategy continues to be valid, with expectations of future government subsidy funding being confirmed in this year's draft settlement or determination as it is known.

3 Monitoring of the position so far this year indicates that the budget could be underspent by around £0.2m. This year's variance is made up of the following anticipated movements:

Budget variance	Forecast year end £000	One off / Ongoing	Comments
Housing Revenue Account			
Repairs account	**(121)	One off	* See commentary at 4 below
Derby Homes Management Fee	80	One off	Additional Management fee to meet the costs of Alvaston area office closure
Capital Financing Charges	(443)	Ongoing	Lower than anticipated borrowing costs
HRA Subsidy	315	Ongoing	Impact of reduced borrowing costs on subsidy payable
Interest on HRA Balances	(150)	Ongoing	Increased HRA balances has attracted additional interest
Total HRA	****(198)**		** excludes Repairs under spend which will be earmarked

4 Following problems encountered in previous years, the Repairs Account was included in the Council's list of risk budgets. As a result, the account has been monitored more closely than in previous years. Latest forecasts indicate that an under spend of approximately £121k may be achieved in the current year.

5 As part of the review of Local Area offices, the Alvaston office was deemed surplus to requirements. The office was originally two shop premises which were made into one unit, by the Council, to create the Area Office. The shops were leased to the Council and as part of the lease agreement; it was a requirement to return the premises to their original condition – i.e. two shop units. Latest estimates for the costs of this work are in the region of £80k. The management fee to Derby Homes is therefore increased on a one off basis to cover the costs of this work.

6 The HRA, like the General Fund, has to bear the financing costs of its borrowings, used in support of the HRA capital programme. A restructuring of these borrowing costs has led to a reduction in both the current year and going forward.

7 General HRA balances at the end of 2006/07 stood at £13.68m with a further £1.8m of Earmarked funds also held. The general balances were £1.64m higher than was expected due to increased rental income as a result of lower than anticipated stock losses and a reduced contribution to the bad debt provision.

Future planning

8 The HRA budget has to be balanced each financial year, and the Council has to plan for the HRA over a period of thirty years. The proposed HRABP for the next thirty years is set out at Appendix 2. A more detailed budget for the HRA for next year is set out at Appendix 3.

Previous plan

9 In the previous plan, key assumptions were made about rent levels, capital costs and funding, and housing subsidy levels.

- **Rents**: it was assumed that rent restructuring would continue until 2012. It was also assumed that the Council would be fully compensated within the subsidy system for restraining average rents to 5% overall as required by the government, requiring higher rent increases of around 4% above RPI a year after the cap is lifted should the target of 2012 be required to be reached, and that any extension to rent capping would continue to be compensated in the subsidy system.

- **Capital:** it was assumed that the Estates Pride programme would start during 2006/07 and that it would be contained within the £15m provisionally set aside for the programme, and that thereafter costs could be contained within funding levels made available by the government through the Major Repairs Allowance, MRA.

- **Housing Subsidy:** it was assumed that MMAs would continue to increase in real terms by 0.75% a year until 2012, and by 0.5% a year thereafter.

Review of key assumptions

Rents

10 This year's subsidy determination has caused significant uncertainty with regard to rent levels and future funding. Under the previous determinations the rent convergence point was 2011/2012. In the autumn, DCLG went out to consultation on proposals to remove the cap. The options for consideration were;

- Return to basic rent restructuring with deadline confirmed as 2012 or
- Extend the period of rent restructuring beyond 2012 to keep rent increases at a more affordable level

The Council's preferred option was to extend the period of rent restructuring to keep rent increases at an affordable level.

11 The government's proposals for the HRA have been drafted for one year only – 2008/09. The previously imposed a cap on average rent increases of 5% a year for 2006/07 and 2007/08 has now been lifted, leaving Councils in our position – where

rents have fallen behind where they should have been by a long way – in a difficult position. The simplistic solution would be to inflate rents back to the level that they would have been without rent capping, but this would lead to rent increases of an average of 12%. If this is smoothed over the remainder of the original rent restructuring period, the rent increase would be 8%, with increases of 4% above inflation for the next three years as well. A longer period has been assumed – for this year only – by the government in calculating the guideline rent for subsidy purposes. To move to the guideline rent would result in an increase of 7.4%. Clearly the HRA will lose funding as a result of any option short of the first one, which would be unpalatable to tenants and to the Council.

12 Rents have been modeled in the plan at this point on the basis of projected guideline rents, but should another option be chosen by the Council then this plan will need to be amended accordingly.

Capital

13 One of the larger risks in the budget remains the ability to manage to maintain the existing stock within the anticipated funding from the Major Repairs Allowance, MRA, and the existing repairs account. Repairs' spending was under spent last year by £374k; however, this was achieved by unsustainable reductions in service. Derby Homes have expressed their concerns about their ability to continue to deliver reductions of this level on what is already seen as a very tight budget. In addition, it has long been a concern that the MRA alone would not be sufficient to maintain the Decent Home Standard in the future.

14 Following substantial investment in the Housing stock the Council was able to declare its stock decent some 4 years ahead of the target date of 2010. The funding for this investment was a 'one-off' and was designed to achieve the prescribed level of decency - in fact the Council went beyond this by achieving decency plus. However, after this funding ended the only resources available to maintain this standard were the MRA and Borrowing approvals of approximately £1m per year. As mentioned previously, it has long been a concern that these resources alone would make it very challenging to maintain the stock in its present state. Derby Homes have completed an asset management plan that indicates that spending ought to be increased on capital in order to maintain the stock in an appropriate state in the longer term, by around £2.8m a year, in addition to maintaining a £1m a year level of funding supported capital, currently expected to end around 2013/14. The impact of such an increased level of spending can be seen in Appendix 4, where a sum of £3.8m to continue to maintain the stock at a 'realistic lifestyle' level has been added to the total spending indicated in our balanced plan starting in 2012/13. Unfortunately this level of spending is clearly unaffordable, with the HRA moving immediately into yearly deficits, and running out of funds within 4 years, and with a deficit of around £209m at the end of 30 years. There now appears to be some doubt as to whether the £1m a year borrowing approval will continue to be allocated by GOEM. If this is the case, these figures will be even worse.

15 If the option of 'opting out' of subsidy arises, it is therefore at face value a tempting thought to avoid such a scenario. The Council will of course continue to monitor developments in this area, but the current discussions are around 'fiscally neutral' options which could in effect mean locking into assumptions about the future that are similar to the expected track of subsidy. On the current assumptions, therefore, this option is unlikely to offer significant benefits to the Council nor tenants.

Estates Pride

16 The Estates Pride programme is revenue funded by the HRA and can therefore be used on either revenue or capital. It can be used in a completely flexible manner, with no time, revenue or capital constraints. This ability to be used flexibly has been particularly helpful when considering external matched funding bids which are often set against very tight timescales and where it is normally difficult to find the funds to allow the matched funding to be offered, thus attracting the grant.

17 The total approval to the programme last year amounted to some £9.045m of both capital and revenue schemes. Revenue resources of £3.5m were already committed for five years to both neighbourhood working and a youth inclusion programme. The balance of £5.545m were committed to a series of developments, including supporting the Street Lighting PFI project from 2007/08, contributions to proposed grant schemes and a sum of £0.76m for Derby Homes to allocate to the greatest priorities that it identified.

18 Given the serious reduction in funding as a result of the proposed level of housing subsidy for next year and the implied future track of subsidy, there might be a case for restraining the level of spending on the Estates Pride programme. For the moment, the plan continues to assume that the full £15m can be supported, but it would be possible to reduce this level of spending and use the funding for more direct investment in the future. To date approximately £9m of the total has been either committed or spent, and the original plan was for the balance to be committed over the next two years. This is therefore really the last chance to significantly alter the balance of the programme if that was desired.

	Latest Approved Budget	Revised Budget
Already Committed	£000	£000
Five year revenue programmes (total committed over five years)		
Neighbourhood working	2108	2108
Youth Inclusion Project	1000	1000
One off issues:		
Street Lighting Contribution	1210	975
Contributions to capital schemes	502	502
Balance for capital works including management of the programme	1525	1525
Additional Contributions to capital schemes	1050	1285
Physical environmental improvements	1700	1700
Funding Committed to 2007/2008	**9095**	**9095**
Further proposals to be considered		3000
Total commitment at this point	**9095**	**12095**
Projected funding available	15000	15000
Balance for later projects assuming funding remains available	5905	2905

Housing Subsidy

19 The future track of housing subsidy appears to be that it will continue to worsen each year. The national HRA has now moved into surplus on all measures, and if current policies are maintained, will move into greater surplus each year, as rents now exceed all forms of spending within the national HRA. Derby's own subsidy remains a positive amount for now, but will become negative in a few years' time. Once rents have converged with RSL rents at some point, current expectations are that rents will continue to increase in line with RSL rents – that is at 0.5% above the rate of inflation. This gives the government more resources than it costs to increase the Management and Maintenance Allowances, MMAs, and the Major Repairs Allowance, MRA in line with inflation. During rent restructuring, the government has been recycling an element of these additional resources back into MMAs to allow some limited real terms growth in funding. Unfortunately, this level of 'rebasing' as it is known, has been reduced to only 0.2% this year.

20 Once rent restructuring is complete, the government's policy appears to be that no further rebasing will take place. The current plan in Appendix 2 is set on the basis that post rent restructuring, there will continue to be some rebasing of around 0.4% a year. Should this not take place, then the position would be as set out in Appendix 5 – with a less sustainable financial position for the HRA in the longer term, with the HRA moving into annual deficit in around 16 years time, and into overall deficit in about 28 years time. The level of risk is therefore less than that surrounding the cost of maintaining the stock itself, but still material. If this scenario came about, then further efficiencies would be required at some point in the future before the HRA goes into significant deficit.

Derby Homes' management fee

21 The basic principles of setting Derby Homes' management fee remain the same as previously agreed, and involve an increase for inflation of 3% and reductions relating to the number of homes no longer managed by Derby Homes, and the ending of a number of older leases.

22 The fee for 2008/2009 includes a one-off increase of £285k, which is the Council's contribution towards the costs of a replacement Housing Management system for Derby Homes. The HRA strategic working party recommended that the Council meet half the costs of this development in the form of such an increase.

23 In addition, two other specific increases are proposed to the fee for next year. Firstly, a commitment to increase the fee commensurate with any increase in employers' pension contributions as a result of LGPS contributions relating to staff transferred from the Council. An illustrative figure of £191,000 a year has been included, but it is hoped that a lower figure should be required when the final contribution rates are made known by the County Council's actuaries. Funding for this purpose will equally be reduced when the contribution rate falls in the future as the deficit on the fund is eventually erased.

24 Secondly, there is a commitment to continue funding social activities within sheltered housing now that the warden service has been restructured as a consequence of Supporting People funding changes. As a result, £58,000 has been added to the

base management fee. No increases are proposed in the retained HRA budget apart from a contingency to cover potential increased costs as a consequence of job evaluation. As yet this is unclear and so a contingency of £100,000 has been added until the position is clarified.

25 Appendix 6 sets out the fee proposed for Derby Homes for the next three years.

Conclusions

26 The latest determination from the government has made the outlook for the HRA very uncertain indeed. The proposals in this consultation suggest continuing with the current policy and maintaining the estates pride programme to its conclusion, despite the loss of funding as a result of the ending of the rental constraint allowance that used to compensate us for the loss of rental income as a result of rent capping. This involves a risk in terms of assuming that real terms increases will continue in future. Should this not be the case, the HRA could face considerable downward pressure on spending at the same time as continued upwards pressure on rents.

27 Whether the funds set aside for long-term maintenance and repairs will be sufficient to maintain the standards that have been set by the Homes Pride programme in the longer term is a considerable risk to the HRA. The reliance on MRA might prove to be inadequate in the future, and the repairs account continues to be under significant pressure.

28 There is an assumption within the given figures that the government will be able to afford to recycle or 'rebase' funds into MMAs from the increase in rents nationally. This has been assumed as 0.2% a year above inflation for the next few years, and 0.4% thereafter. There is a risk that the government may not continue to abide by these promised levels of funding at some point in the future. Should this happen there would be a significant problem for the HRA at that point, as funding would cease to increase in real terms per home in the way that it has for the last few years, and is projected to continue.

Consultation

29 This consultation paper is being widely distributed, including to Derby Homes' Board and its senior management, tenants through consultative bodies, and the Community Commission.

For more information contact:	Officer: David Enticott Tel 255318 e-mail david.enticott@derby.gov.uk
Background papers:	Draft determination of Housing subsidy and related emails.
List of appendices:	Appendix 1 – Implications Appendix 2 – HRA business plan Appendix 3 – HRA budget 2008/9 Appendix 4 – HRA business plan with Asset Management spending increased Appendix 5 – HRA business plan without rebasing after rent restructuring Appendix 6 – Derby Homes' management fee

IMPLICATIONS

Financial

1. Set out in the report.

Legal

2. The Council is required to set a budget for its Housing Revenue Account that balances and that charges costs appropriately to either the HRA or to the General Fund.

Personnel

3. None directly.

Equalities impact

4. Many of the Council's tenants belong to the Council's equality target groups.

Corporate objectives and priorities for change

5. The objectives of **making us proud of our neighbourhoods, leading Derby towards a better environment and giving you excellent services and value for money** are all enhanced by the improvements in council house standards as a result of Decent Homes, and by any improvements possible through the Estates Pride programme, as well as through other services and investments made possible through the HRA.