DERBY CITY COUNCIL

COUNCIL CABINET
16 FEBRUARY 2010

ITEM 28

Report of the Corporate Directors of Corporate and Adult Services and Resources

Housing Revenue Account Business Plan and Budget 2010/11

SUMMARY

1.1 The Housing Revenue Account, HRA, remains financially robust in the short term but continues to face increasing pressure over time. The HRA has a long-term planning framework, with a three-year budget supplemented by a thirty-year business plan, known as the HRA Business Plan, or HRABP.

1.2 The government's long-term review of the HRA Subsidy system, HRAS, undertaken last year concluded that there was an urgent need for reform. The government intends to make an offer to local authorities at some point this month setting out terms under which the Secretary of State would be willing to agree to an authority being able to be excluded from the HRAS system in future. This is likely to take the form of an additional – or in a few cases reduced – debt to be placed on the HRA in exchange for ceasing to include that Authority in the HRAS system in future.

1.3 The exact format or content of that offer remains unknown but could have a significant effect on the future of the HRA. It is hoped that the format and content of the offer will be acceptable and lead to many acceptances of the offer across the country, bringing the HRAS system effectively to an end. This outcome cannot be guaranteed however, and it remains unclear at this point.

1.4 In the meantime, there is a need to consider the situation as it stands, and also in the event that this process is not successfully concluded. As a result, there remains a need to set out a further plan on the existing basis under the HRAS system.

1.5 It is not proposed to change the business plan radically, but to make moderate improvements to funding in a few areas, concentrating mainly on the repairs account which has come under significant pressure over recent years.

1.6 The proposals contained within this report approve a slight reshaping of the final year of the Estates Pride programme of works, completing the £15m total programme that has been running now for four years. By the end of this year, it is estimated that the Council will have spent £7.7m of this programme and the remainder will be spent over the next few years on the programme that has already been largely agreed. Consideration needs to be given to the impact that the ending of this programme will have if alternative funding is not forthcoming as a result of the HRA review.

1.7 There are also other funding sources that are no longer being received and will impact on the plans in the medium term – primarily the funding for the aids and adaptations budget that effectively came from the Supported Capital Expenditure approval of £1m a year that has now ceased and that has been supported for the last few years from HRA reserves.

1.8 New Service Charges are proposed for grounds maintenance and for smoke alarms. These will raise significant funds over time and allow greater investment in future in capital and repairs than would otherwise have been the case. They will also eliminate existing cross subsidies between tenants under the current arrangements. In 2010/11, all tenants will pay no more than they would have done had these charges not been introduced by means of a reduction to their rent.

1.9 Despite the proposed generation of additional funding, there remains a series of additional pressures that are not covered in the proposed, including an estimated additional need of around £400m over the 30 year planning period for major investment. A summary of the main unfunded pressures on the HRA from 2011/12 onwards is shown in section 10.1 below.

RECOMMENDATIONS

2.1 To approve the budget set out as part of the HRA Business Plan at Appendix 2 and detailed in Appendix 3 which are available on CMIS.

2.2 To approve the revised proposals for Estates Pride as set out in Appendix 4, which is available on CMIS.

2.3 To approve the management fee for Derby Homes set out in Appendix 5, which is available on CMIS.

2.4 To make the repairs budget available to Derby Homes to meet their costs in providing the repairs service.

REASON FOR RECOMMENDATIONS

2.5 The longer term funding position of the HRA is much less attractive than the current position as the HRA is set to lose in excess of £5m a year of housing revenue account subsidy from 2011/12. At this point, services would suffer a huge downward budget pressure if pro active action had not been taken over the last few years. As a result, the HRA has been building up reserves to allow it to be able to mitigate the worst effects of that loss of funding.

2.6 The hope remains that the imminent offer to opt out of HRAS might enable additional investment for the future, although the short term impact could be less beneficial or even negative in order to reach the future benefits that might arise in the medium term.

SUPPORTING INFORMATION

Review of HRA financial position 2009/10

3.1 The aim of the Housing Revenue Account, HRA's, financial strategy for the last five years has been to generate sufficient funding in the short term to allow a relatively smooth transition after the ending of substantial additional ALMO funding in 2011/12 of over £4m a year. In addition, the strategy involves the maintenance of an Estates Pride fund of £15m for improvements to estates and facilities available for the benefit of tenants.

3.2 This strategy continues to be valid. The strategy is likely to require revising once the imminent offer to opt out of the HRA Subsidy system, HRAS, is made later this month. In the meantime, the strategy is based on the HRAS continuing as it is currently formulated, with increasing subsidy withdrawals over time.

3.3 The previous business plan approved last year anticipated that HRA expenditure would exceed income by around £5.6m as a result of the total additional investment of £7.3m from reserves into specific capital investments previously approved. While this investment is being made as speedily as possible, the scale of the additional investment has led to about £4.4m of this funding being profiled to be spent in 2010/11 rather than 2009/10.

3.4 The latest projection indicates an in year deficit for 2009/10 of around £1.2m, but with an increased deficit in excess of £4.0m in 2010/11 - as the committed additional capital is spent. The reserves are anticipated to fall to around £7m by the end of 2012/13, even with the planned additional income set out in the rent report elsewhere on the agenda. Depending on the terms of any offer from government with respect to opting out of HRAS, it is possible that a considerable proportion of these reserves could be needed to deal with the short term implications of that offer. This will need to be reviewed when the offer is clarified soon.

3.6 The longer-term position remains broadly as in previous years. From 2011/12 we start to have to pay a significant sum in negative subsidy - over £5m, and this increases by about £1m a year thereafter.

Future planning

4.1 The HRA budget has to be balanced each financial year, and the Council plans for the HRA over a period of thirty years.

4.2 The proposed HRABP for the next thirty years is set out at Appendix 2 which is available on CMIS. A more detailed budget for the HRA for next year is set out at Appendix 3 which is available on CMIS. The basis on which these have been produced includes income raised by the introduction of service charges elsewhere on this agenda, and the utilisation of that income largely on additional capital investment.

4.3 The longer term position is that a substantial increase in funding is still required to make the overall position sustainable. This deficit would be of the order of £400m over the plan, and a substantial reworking of the current plan will be necessary.

Previous plan

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

- **Rents**: it was assumed that the government would manage to complete restructuring of rents in 15 years as suggested by them last year.

- **Capital:** it was assumed that the Estates Pride programme would be contained within the £15m 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, albeit supplemented until 2010/11 by £750,000 a year from HRA balances. In addition, further funds were made available for a two year programme of further additional investment in accelerating heat lease replacement and insulation.

- **Housing Subsidy:** it was assumed that Management and Maintenance Allowances would continue to increase in real terms by 0.1% a year during rent restructuring, and by 0.4% a year thereafter.

Review of key assumptions

Rents

6.1 This year's subsidy determination has set out that nationally guideline rents will increase by 3.1% in 2010/11. Derby's guideline has increased by 3.6%. Average actual rents are likely to increase by around 2% as a result of the operation of a cap to rent increases for many tenants. A separate consultation has taken place on a proposed increase in rents for 2010/11. The date of convergence has been brought forward markedly this year to 2012/13 as a result of the low level of RPI inflation. It is reasonably likely but by no means certain that the timetable for rent restructuring will slip again next year. The plans, however, are based on the current government plans for restructuring to be largely completed by 2012/13.

6.2 The government's proposals for the HRA have again been drafted for one year only.

6.3 The closing of the rent restructuring gap over two years – as implied by the government's new target date for rent restructuring of 2012/13 - implies real terms increases in excess of 4% a year, for those two years. The alternative would be for the government to impose lower increases over a longer period – for instance 2.5% a year in real terms for perhaps 4 years. In any event, individual tenants will be at different points on this path – we have a few that are already at formula rent while many others are a long distance from the target – and will all move at an individual pace to the overall formula rent target. Some will take longer than the target date to reach convergence as a result of rent caps which restrain the additional income that can be raised in any one financial year.

6.4 Service charges - if approved in a separate paper on this agenda – are critical to sustain the proposed financial position of the HRA set out in this report. Without this additional income in excess of £1m a year - largely paid for from Housing Benefit – the additional funds proposed could not be afforded. This additional income will cost very little to tenants in the short term, as the operation of unpooling service charges and the rent cap next year means that the overall cost would be the same as it would have been without the charges. For most tenants facing additional service charges this will remain true in the second year as well. Without these funds, there would be need to revisit the existing proposals and to reduce the level of spending.

6.5 There remains a longer term problem even with these additional charges, with some key budgets that are currently unfunded from 2011/12 onwards. Major priority items that require additional funding from 2011/12 are listed at 10.1 of this report. At this point, though, it is hoped that this can be financed from the benefits of being removed from the HRAS system, and it is appropriate to await these proposals before committing to further charges or further spending changes.

Capital

7.1 The biggest risk in the budget remains the ability to maintain the existing stock within the anticipated funding from the Major Repairs Allowance, MRA, and the existing repairs account in the longer term. The loss of Supported Capital Expenditure (Revenue) or borrowing approvals of £1m continues to be a blow to the longer term sustainability of the capital programme, particularly as this had previously been used to fund adaptations to homes for those requiring this investment. The previous plans did not cover any specific funding at all for aids and adaptations beyond 2010/11 – these proposals will rectify that position.

7.2 The HRABP now assumes that funding of £750k will continue to be made available from reserves to maintain the programme of adaptations for 2010/11, but that thereafter this funding will be maintained.

7.3 In the longer term, maintenance of the decent homes standard will become difficult in some homes without increased funding. As a result of an updated stock condition survey undertaken this year, we now anticipate that around an additional £400m over the period of the plan will be needed to maintain homes on a long term basis above the level of funding currently provided for in the plan.

7.4 Last year it was agreed to invest an additional £7.3m in total into the HRA using reserves to accelerate the ending of the heat lease programme and to invest further into the stock – in particular additional insulation works. This spending will spread across two financial years – 2009/10 and 2010/11 – and remains committed in the proposed plans.

7.5 Given the scale of additional investment already committed to, and the nearness of any offer to come out of the subsidy system, which might require the Council to fund short term losses of funding from HRA reserves in order to benefit from a longer term gain, it is not proposed to commit at this stage to further spending beyond the additional investment already agreed and the aids and adaptations increases already mentioned. Once the offer has been clarified, there will be an opportunity to reconsider the position.

Repairs Account

8.1 The repairs account has been struggling financially for a number of years and is again likely to overspend. Part of the problem stems from the balance between management and maintenance overall – management costs are about average while maintenance costs are considerably lower than average. There is therefore an acceptance of the need to rebalance the total spending between these two areas by increasing repairs and major investments over time to a more sustainable total. The aim is that the vast majority of any increased resources that might be available in future - through either the opt out of HRAS or through the current system - for instance from service charges - are therefore focussed on the maintenance part of this equation. This also applies to the increase in management and maintenance allowances which it is proposed to concentrate on maintenance as much as possible.

8.2 In order to tackle this issue, the following actions are proposed this year …

- A 3% increase to the base calculation of the repairs account rather than the 2% increase received in HRAS.
- £35,000 additional resource to cover the increased gas heating checks required as a result of increasing that replacement programme.
- £160,000 additional resource to cover the increased costs resulting from an increase to the home decoration service over the last few years, bringing this funding up to match the expenditure incurred.
- A further £50,000 real terms increase. The last three of these increases are funded by a reduction in expected inflation in pay awards to a much lower level than previously anticipated, consistent with other Council budget planning.
- Consulting on the transfer of DSO staff. This will allow Derby Homes to manage the staff directly and to implement efficiency improvements directly, and have direct control of costs incurred. A separate paper on this issue is being prepared by Environmental Services. The repairs account would need to be made available to Derby Homes to enable them to manage their costs as a result. The expectation is that additional efficiencies can be achieved from within the repairs account as a result.

8.3 These actions amount to a considerable boost to the repairs account, and should tackle the existing problems. The longer term solution would ideally have at least another £1m a year of spending. This level of additional investment is clearly not affordable under the current system, but remains one of the key priorities for any additional resources in the future. The package of measures taken together with direct control of the contractor by Derby Homes should enable a significant improvement in the position of the repairs account next year.

Estates Pride

9.1 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 limits, revenue or capital constraints.

9.2 2010/11 is the last full year of the programme which is now fully committed. There are a few programmes which will last a little longer than the new financial year, funded by brought forward funding within the original total of £15m. From 2011/12 a series of funding streams will end, including funding for neighbourhoods of £262,000 in 10/11, about half of the Enthusiasm project funding – reducing to £109k in 11/12 from £212k in 10/11 and most of the estates improvements themselves for which additional funding will no longer be possible from 11/12. The full proposals for further spending are set out in Appendix 4 which is available on CMIS.

9.3 In addition to this funding ending, the £106,000 a year transferred to support the tree maintenance programme will also run out. Unless alternative funding is arranged then this support will also be reduced from 2011/12.

Pressures on the current plan not covered at present

10.1 To summarise, the business plan has been updated to include income from service charges as proposed, and to finance additional spending on repairs and aids and adaptations. In addition it is proposed to sustain the current investment in additional tree maintenance that would otherwise come to an end after 2010/11. There remain, however, significant issues that remain unfunded from 2011/12 and onwards within the current plan and need to be addressed - perhaps through HRAS changes if agreed. These include:

- repairs - £1m a year more
- general maintenance varies year by year - up to £10m a year additional
- estates Pride any continuing support desired in this area – current plans will cease after 2010/11 – plans set out in Appendix 4
- real terms increases to Derby Homes' management fee to meet any future agreed new pressures.

10.2 In this context, considerable additional funds will be needed after 2010/11 to sustain the service going forward. An estimate of the need over 30 years is around £1.2bn. The current system might provide about £800m, so there is a shortfall of around £400m against a fully sustainable plan. If not addressed, this deficit will begin to build up a backlog of major repairs and maintenance issues. This is the key reason why it is hoped that the imminent offer from government to opt out of the HRAS system will be an adequate one, and that it will release sufficient resources to deal with these problems. Taking on additional debt as part of that offer will have its own costs, but there remains considerable hope at this point that at least some additional funding will be possible through the offer towards reducing this funding gap.

10.3 The short term impact of accepting any offer, however, is quite hard to gauge at this point. It is anticipated that there could in fact be an increase in costs in the short term, drawing down HRA reserves quite sharply. It is therefore critical at this point to maintain HRA reserves at the current planned level – which are currently set to fall to around £7m - in order to be able to take up the offer if the longer term benefit greatly outweighs any short term cost. This was the case in some early illustrative figures. It remains the case that the details of the offer are as yet unknown. It is suggested that further additional investment not be made at this point in order to gauge the offer and any requirements to utilize reserves in taking up any appropriate deal.

Housing Subsidy

11.1 The future track of housing subsidy remains that it will continue to worsen each year as rents increase by more than spending allowances. The national HRA remains in broad balance for now, but 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 about nil for 2010/11m but will become a significant negative amount – likely to be in excess of £5m - from 2011/12 onwards.

11.2 The government is about to issue an offer to individual Councils to opt out of the Housing Revenue Account Subsidy system. Such an offer, depending on the conditions attached, could be attractive in terms of our ability to manage our own stock in future. Initial figures considered by the HRA Strategic Working Party have indicated a considerable improvement on the current position over time, and it is hoped that the final offer will be similar or better. The essential offer is to take on additional debt rather than to continue in the HRAS system. If the costs of servicing that debt are considerably less than our estimates of subsidy payments, additional resources will become available, hopefully reducing substantially the funding gaps indicated at 10.1 above.

11.3 It is not known what conditions might apply to this offer and separate consideration will have to be undertaken to review whether to accept or reject the offer. At this stage, it is hoped that such an offer could be accepted, but the conditions will be critical in making this judgment within the next couple of months.

Derby Homes' management fee

12.1 The basic principles of setting Derby Homes' management fee remain the same as previously agreed. Inflation has been reduced further to 1% for 10/11 and then 1.5% a year for 11/12 and 12/13, in line with assumptions made in the Council's budget strategy. The 2010/11 base position has been corrected for inflation in 2009/10, as 3% was initially allocated compared to a pay settlement of 1.25%. This results in a reduction in the fee of £190,000 a year which has been used to increase the funding available to the repairs account. In addition, the management fee is also reduced to take account of the number of homes no longer managed by Derby Homes, and the ending of a number of older leases.

12.2 It is not proposed to clawback the overpayment of fee for 2009/10 itself in recognition of the investments that Derby Homes have made in assisting the Council with the transfer of some properties for those with Learning Difficulties from the NHS (£125,000) and a contribution to the repairs account (£100,000).

12.3 Given the outlook and the existing pressures, no additional amounts are proposed to be added to the fee at this stage, nor are any reductions proposed to assist with rebalancing the HRA until the outcome of the HRA review makes the longer term clearer. Any requests from Derby Homes will need to be considered against the other pressures noted at 10.1 above at that point.

12.4 Appendix 5, which is available on CMIS, sets out the fee proposed for Derby Homes for the next four years.

Conclusions

13.1 The longer term financial position for the HRA remains very difficult, but the short term financial position of the HRA remains robust thanks to the additional ALMO funding which has supported the Estates Pride programme for the last few years.

13.2 The reliance on current capital funding is likely to prove to be inadequate in the future, and the repairs account continues to be under significant pressure. There are no funds from reserves set aside to support capital after 2010/11. There are a long list of pressures to be funded from 2011/12 onwards that are currently not included in the plan. Service charge income is proposed in order to support the HRA.l.

13.3 There is an offer due from the government relating to opting out of the HRAS system due imminently. This could provide additional resources as well towards a looming longer term funding problem which is getting much nearer now, as the end of considerable additional ALMO Round 1 funding appears to be imminent from 2011/12.

Consultation

14.1 A consultation paper on these issues has been widely circulated, including Derby Homes' Board and its senior management, the City Housing Consultative Group, Derby Association of Community Partners, and the Community Commission.

For more information contact:	Officer: David Enticott Tel 255318 e-mail david.enticott@derby.gov.uk
Background papers:	Determination of Housing subsidy and related emails. Consultation papers on rents and HRABP
List of appendices:	Appendix 1 – Implications Appendix 2 – HRA business plan – available on CMIS Appendix 3 – HRA budget 2010/11 – available on CMIS Appendix 4 – Estates Pride programme – available on CMIS Appendix 5 Derby Homes' management fee – available on CMIS

IMPLICATIONS

Financial

1.1 Set out in the report.

Legal

2.1 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

3.1 None directly.

Equalities Impact

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

Corporate objectives and priorities for change

5.1 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.