DERBY HOMES BOARD
28 NOVEMBER 2013

ITEM B3

HRA BUSINESS PLAN AND RENT PROPOSALS

Report of the Director and Company Secretary

1. SUMMARY

1.1 Derby City Council is consulting on both rent increases and the HRA Business Plan (HRABP) for 2014, and is asking for a response from interested parties including Derby Homes' Board.

1.2 The government is also consulting on longer term rent policy for 2015 for 10 years.

1.3 Overall the Council's plans are in line with our joint plans and it is recommended that they be supported by the Board. The government's plans for regulation of rent include an end to rent convergence a year early which threatens the HRA with potential losses of around £1m a year depending on the detailed rules on the limit rent which have yet to be released.

2. RECOMMENDATION

2.1 To consider the Board's response to the Council's proposals contained within their consultations on Rents for 2014 and the HRA Business Plan for 2014/44

2.2 To support Rent Option 3 as giving the best balance between resources available to the HRABP and avoiding excessive rent increases.

2.3 To support the HRABP consultation proposals which would enable the partnership between the Council and Derby Homes to maintain services to tenants and deliver additional affordable homes.

2.4 To approve the draft response to the government's consultation on rents set out at Appendix 1.

3. MATTER FOR CONSIDERATION

3.1 The Council has issued two consultation papers on the HRA Business Plan (HRABP) and Rents and Service Charges as usual each year, inviting comments on their content from interested parties including the DACP and Derby Homes Board.

3.2 The Government is also currently consulting on the future of social rents and a draft response is attached at Appendix 1. The detail of that consultation unfortuneately misses out the future calculation of the limit rent which is critical to Council decisions on rents. This detail is expected in December. The Council's proposals anticipate a possible scenario, necessarily making assumptions about those detailed rules based on the guidance that has been published to date. Clearly the Council will need to take the final guidance into account in finalising their proposals for rents.

3.3 The Council's proposals on rents (attached at Appendix 2) refer to the need to balance the likely rent increase level and the amount of funding available to the HRABP. This is not a new issue, but the government consultation on rents for 2015/16 onwards makes it clear that rents are to be limited to CPI plus 1% in future, and that rent restructuring will therefore come to an end a year earlier than planned. This would leave Council average rents around 3% below the average target rent in 2015/16 and onwards. If this gap is not closed then the HRABP will have fewer funds available for investment in new homes. 2014/15 therefore appears – at this stage and subject to the final details of the limit rent - to be the last year in which a decision on rent levels increasing above this level could be made.

3.4 The Council's paper therefore sets out five possible scenarios for rents, ranging from continuing as planned last year to moving all tenants to target rent. The options are set out below:

Option	1	2	3	4	5
Limit on increase /wk	Last Years over 2 yrs max £2	£2	£4	£6 (limit rent)	Target Rent
Average Rent £/ wk	**76.59**	**77.00**	**77.87**	**78.27**	**79.23**
Average % increase	5.5	6.0	7.2	7.8	9.1
Highest %	8.5	8.5	13.2	18.0	78.5
10^{th} percentile%	5.9	6.1	8.8	11.4	16.2
Rent increase >20%	0	0	0	0	965
Loss of funds	**-1.3**	**-0.9**	**-0.2**	**+0.1**	**+0.5**

3.5 The Council has now had two and a half years of moving new tenants to target rent – so far around 1700 tenancies are now on target rent and their average increase will therefore be 3.7% - that is September's RPI (3.2%) plus 0.5% in all these scenarios.

3.6 Other tenants continue to receive protection through a transition to target rent limited by the rent convergence criteria of RPI+0.5%+ a maximum of £2 a week. In theory the Council could move to the target rent immediately next year – this would maximise the funds available to the HRABP but would place a large number of tenants in a group facing very steep increases to rents – almost 1000 would be facing increases above 20%. Option 4 would move to the limit rent - the long term aim of rent policy - and would balance the plan back to the previous position overall but still mean a rent increase of more than 10% for almost 3000 tenants. Option 3 reduces the number facing an increase of more than 10% to just 600 – about 5% of tenants, and still almost holds the HRABP steady. Option 2 would result in a loss of almost £1m a year, and option 1 would mean a loss of £1.3m from the current plan. Comments are invited on which option to go for.

3.7 In reaching the loss of funds figures above, two HRABP gains have been included – first is the impact of the gain in rent as a consequence of moving new tenants to target rent – this has gained around £0.35m a year in additional rent. A similar amount has also been gained as a result of higher than expected September RPI inflation (3.2% compared to 2.5%). If these factors were removed, then the loss of funds above would be around £0.7m worse in each case.

3.8 From Derby Homes' point of view, maximising the resources within the HRABP is critical to continued successful management and maintenance of the existing stock and to enable the Council to undertake further development of new homes. The Council, Derby Homes and the DACP have all consistently supported increasing the rent as far as pratical within government guidelines towards rent convergence with a view to maximising the resources available in Derby. 56% of rents are currently paid by Housing Benefit with 65% of tenants receiving some or all of their rent from that source. Having said that, increases of the scale that would have to be contemplated for option 5 in particular would be too great for many self funding tenants.

3.9 Option 3 appears to give the best balance between a loss of income that is manageable for the HRA and keeping the rent increase to a reasonable level. Under this option, those on target rent would have an increase limited to 3.7% and individual increases for longer standing tenants would be limited to the £4 above RPI plus 0.5% that would have been expected over the next two years under the previous policy (£2 each year). In effect both years' increase would be applied as a result of the bringing forward of the convergence date by a year. Next year's increase could then be limited to CPI plus 1% as proposed by the government in their consultation. To move to the first two options would lose around £1m a year of HRA funding and would only reduce the average rent increase by just 87p/week for option 2. Rent levels will remain well below market levels – the proposed average rent will be £77.87 a week under Option 3: this year's Local Housing Allowance rate for a 2 bed property is £103.85 a week - £26 (33%) a week more. Rents therefore remain competitive.

3.10 The Board may also wish to support the intention to review Furniture Pack charges and to freeze them this year.

HRA Business Plan

3.11 The consultation on the proposals for the HRABP (attached at Appendix 3) has been drawn up on the basis of Rent Option 3 as a working assumption, and would have to be adjusted if a lower increase in rents were to be selected by the Council.

3.12 In general, the plan is consistent with previous years but makes further proposals in the following areas:

- To delegate the payment for HRA grounds to Derby Homes along with a fee increase
- To consider increasing the management fee by £0.2m a year to help Derby Homes to sustain the Intensive Housing Management service replacing the supported living service
- Allocating up to £50k of the Estates Pride programme towards funding the Crime Prevention Team taken on by Derby Homes this year.
- Making the final reduction in Derby Homes' management fee of £250,000 to complete the budget reductions under Business Transformation. We have already delivered these savings.

3.13 These developments, if approved, would allow Derby Homes to set aside funding to support new properties of our own to complement Council and other Registered Provider development across Derby as planned, using the efficiencies planned within our budget and that are currently running ahead of target. The new build programme is critically dependent on the management and maintenance fees being maintained under the existing formulae and not reduced further. Should any further reduction take place, Derby Homes' capacity to deliver new homes would be reduced.

3.14 Overall, the HRABP proposed supports the joint ambitions of the Council and Derby Homes to deliver more homes to replace as many of those lost through the Right to Buy as possible, to maintain standards of existing homes and provide good housing management services to tenants. Support for the Council's plans is therefore recommended.

4. CONSULTATION IMPLICATIONS

Consultation with the DACP, Derby Homes Board and the Planning Housing and Leisure Board is planned by the Council. Derby Homes will support the Council in this process as required.

5. FINANCIAL AND BUSINESS PLAN IMPLICATIONS

The HRABP is critical to Derby Homes as it is the source of the vast majority of our income. Rent levels are critical to the HRA as it is the source of almost all the income that funds the HRA. 56% of rent is met by Housing Benefit, and as a consequence, it is important that the maximum level of rent is set that is consistent with reasonable increases for tenants that are currently facing lower than target rent levels – that is tenancies starting prior to April 2011. Under Option 3 these tenants would face the equivalent of the increase of £4 (£2 a year for 2 years) above RPI+0.5% each year in one go rather than over two years as previously planned as the government has indicated that such an increase will not be possible next year. If approved this would result in only marginal long term rental losses for the HRABP. Lower increases would probably result in lower levels of development.

6. COUNCIL IMPLICATIONS

This is a matter which requires the approval of the Council. Approval will be sought at the meeting of the Cabinet in February 2014.

7. PERSONNEL IMPLICATIONS

Should the plan to support the new Intensive Housing Management resource not be approved there could be implications for the structure of housing management. If approved, staffing numbers are expected to fall gradually with staff turnover over the next year or so.

8. EQUALITIES IMPACT ASSESSMENT

- Does this report affect the delivery of a service Yes
- Has an Equality Impact Assessment been completed No (please attach as appendix)
- If no Equality Impact Assessment has been completed please provide a

summary of the equalities implications – Delivery of additional homes for tenants will help with provision of affordable housing for Derby.Some homes may be targeted at specific groups with particular needs.

9. RISK IMPLICATIONS

The HRABP has a separate risk register and also impacts on Derby Homes income prospects. Support for the plans as drafted would enable plans to continue and for risk to be mitigated through sufficient funding for the plan.

The areas listed below have no implications directly arising from this report:

Legal and Confidentiality
Environmental
Health & Safety
Policy Review

If Board Members or others would like to discuss this report ahead of the meeting please contact:

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Background Information:	Government Social Rent consultation https://www.gov.uk/government/consultations/rents-for-social-housing-from-2015-to-2016
Supporting Information:	Appendix 1 – Draft response to Rent consultation Appendix 2 – Rent consultation Appendix 3 – HRABP consultation

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Appendix 1

Draft response to Government Social Rent consultation

Question 1: What are your views on the Government's proposed policy on social rents from 2015-16?

While there are positive elements to the policy (see q3), there is a real problem with the proposal to end rent convergence a year early. Derby has followed government guidance in setting rents and despite this they remain well below target rent at this stage (5.5%). It was intended that the majority of the balance would have been caught up over the next two years - but also that a longer period would be given to those tenants that were further away from target rent – so that tenants rents would continue to increase at a maximum of £2 above RPI+0.5%. Again this was the level set in the debt settlement and has continued to be applied. It is not reasonable therefore to suggest that landlords should have dealt with this by now. The implication of this is that we should not have followed government guidance and should have increased rents faster earlier. This is not a position with which we can agree. We would urge that the government honour its promise to Councils and their tenants that rents can increase at a rate limited at a similar rate to that previously agreed.

Clarity on how the limit rent is to be set in future is needed soon to assist Councils to set rents for the longer term.

Question 2: Should the rent caps be removed? If you are a landlord, how (if at all) do the caps impact on you currently?

Not applicable in Derby

Question 3: Do you agree with the move from basic rent increases of RPI + 0.5 percentage points to CPI + 1 percentage point (for social rent and affordable rent)?

Derby Homes welcomes the certainty that the government has brought to medium term rental planning through its proposals for rents to be limited to increases of CPI plus 1% a year for the next ten years. Previous policy was open to being amended and a longer term perspective is important for making longer term decisions such as investing in new homes.

We are disappointed that the previous arrangement of RPI+0.5% has been replaced by CPI+1% as this is expected to be a materially lower level of rental income which will impact on the capacity of Councils to deliver additional housing. The expected gap between the two inflation measures of around 1% is clearly not reflected in the new arrangements – CPI+1.5% would have been closer to an equivalent according to the Treasury's impact assessment. RPI+0.5% was assumed in setting the debt levels taken on by Councils and such a material adjustment ought to lead to an adjustment to debt levels. Having said that, HRA plans have been set at inflation levels of 2.5% long term and if CPI is around 2% in the longer term and costs are controlled to inflation then plans should still be broadly sustainable. It is just a shame that the further development that might have been supported through an RPI link will be restricted as a consequence of this and the debt cap.

Question 4: Do you agree with the definition of "household" proposed'?
Question 5: Do you agree with the definition of "income" proposed?
Question 6: In particular, should capital be included and if so, how?
Question 7: Do you agree with the income period proposed?
Question 8: What are your views on the proposed self-declaration approach?

No comment on these issues related to high income tenants – we don't believe we have many (or possibly any) and it is unlikely to be a major issue but could be a considerable administrative burden if we are required to check household income levels. In any event, increasing the rent to a market level would be likely to prompt a Right to Buy application from a tenant who was able to continue to be subsidised in that way instead of through rent.

Question 9: Do you agree with how we propose to treat historic grant?

Yes – retaining HCA grant in the property makes sense.

Derby City Council

Rent Increase 2014/15

Consultation on proposals for Rents and Service Charges

Derby City Council's current policy with respect to rents is to follow the government guidance on rent convergence and to comply with the current limitation on increases in any one year for individual tenants to a maximum of RPI+0.5%+£2 a week.

Under previous plans, this would have meant that existing tenants would have annual increases restricted as above, but eventually all rents would reach the government formula or Target Rent levels. The timetable had been to reach this level in 2015/16 – meaning that there was two years left to close a gap between target rent and actual rent levels, which on average is currently 5.5% (just over £4 a week).

The government has now published a consultation on rent levels for the longer term which proposes to change the formula for increasing target rent each year from RPI+0.5% to CPI+1%. While this change does reduce the long term income that the HRA is likely to receive (the long term difference between RPI and CPI is around 0.7% to 1%), it does mean that the business plan is relatively unaffected. Current plans are based on the government target for RPI of 2.5% and this will change to the CPI target of 2% - leaving the underlying increase in target rents unaffected at 3% a year.

The second proposal from the government is to stop rent convergence after only one more year rather than two years. This means that the Council is likely to have only one more chance to close the gap (2014/15) as from next year (2015/16) individual rents will be limited to a CPI+1% maximum increase.

The details of government regulation of rents are likely to be released in December and are not available at the time of writing this paper. They may impact on the final decision of the Council Cabinet which will be in February 2014 as normal.

Subject to the detailed regulations, the Council may have to choose between the following options to increase the rent:

	Annual Impact £m	Average %
1. Sticking to first year of the Current plan	-1.3	5.5
2. Increasing by full £2 limit where under target	-0.9	6.0
3. Increasing by £4 (2 years of £2) where under	-0.2	7.2
4. Moving to the limit rent #	+0.1	7.8
5. Moving to target rent	+0.5	9.1
Target Rent		3.7

The impact on the business plan is less in all cases than might have been expected as the RPI for September 2013 was 3.2% rather than the expected figure of 2.5% in the business plan. Tenants already paying target rent (including all those with tenancies since April 2011) will see increases of 3.7% in line with target rent under all options above.

The limit rent is the point at which the government will claw back most of the income raised through rents – there is therefore little gain in charging much above this level. The government have yet to determine the level of the limit rent for next year, so this is an estimated level. Increasing the rent to this level would leave around 2,800 tenants facing an increase over 10% in their rent.

Moving to Target rent in one go would mean that almost 1000 tenants faced an increase above 20% in rents and another 1800 have increases above 10%. For this reason, option 5 above is not likely to be supported.

In terms of the business plan, Option 4 would generate enough money to support the full previous plan, Option 3 would generate almost as much. Options 1 & 2 would provide substantially less and would reduce the funding available to be put into new build replacements in the longer term.

Option 3 appears to give the best balance between a loss of income that is manageable for the HRA and keeping the rent increase to a reasonable level. Under this option, those on target rent would have an increase limited to 3.7% and individual increases for longer standing tenants would be limited to the £4 above RPI plus 0.5% that would have been expected over the next two years under the previous policy (£2 each year). In effect both years' increase would be applied as a result of the bringing forward of the convergence date by a year. Next year's increase could then be limited to CPI plus 1% as proposed by the government in their consultation. To move to the first two options would lose around £1m a year of HRA funding and would only reduce the average rent increase by just 87p/week for option 2. Rent levels will remain well below market levels – the proposed average rent will be £77.87 a week under Option 3: this year's Local Housing Allowance rate for a 2 bed property is £103.85 a week - £26 (33%) a week more. Rents therefore remain competitive.

Service Charges
It is intended that service charges be increased by inflation of 2.6% with the exception of furniture packs which could be frozen for next year and will be the subject of a separate review.

Comments are invited on which option would be preferred to inform the Council's decision.

HRA Business Plan 2014/44

Executive Summary

The HRA has now had 18 months since the debt settlement of 2012 which gave Council Housing a sustainable financial position for the future, but it now faces a number of challenges:

- **Welfare Reform** – Universal Credit's impact on rental income collection and collection costs, the underoccupation charge, personal independence payments replacing disability living allowance – each of these will result in higher bad debt levels and arrears
- **Likely constraints on Rents** – details are awaited, but there appears to be a likely constraint on increasing rents according to the settlement agreed in 2012 – rent convergence is to be stopped a year early. This will impact on rent and income levels.
- **Continued Right to Buy losses** – the level of sales is slightly higher than anticipated this year and is likely to increase still further as a result of the proposed reduction in qualifying time to three years (currently five).
- **The debt cap** – while not an immediate issue, continuing to reinvest RTB funds and match them with new borrowing will mean that debts increase towards the cap and will constrain development of new homes eventually. The HRA Business Plan remains robust overall and could potentially sensibly manage to deliver more homes with a higher debt cap.
- **Service Charges -** there is a further potential impact of Universal Credit (UC) on the type of service charges that can be levied in future once UC is operational – some may no longer be recoverable but others may be. This is an issue for the future.

The partnership of Derby City Council and Derby Homes remains strong and focussed on delivery of new homes through that partnership. The HRA and Derby Homes both have plans to deliver additional homes and to add to the stock of well managed affordable homes in Derby.

Overall, the plan suggests that – as a result of the likely constraint on rents – there will be a reduction in the ability to invest, but that there remains capacity to deliver 400 homes through the HRA over the next few years, and around 50 to 60 a year thereafter. The core service to existing tenants should remain at its current level, with homes being actively managed and maintained to a decent standard.

This report is much briefer than previous years – in order to try be more concise and remain focussed on the key issues.

Overall approach

The Council and Derby Homes remain committed to maintaining value for money for tenants, maintaining homes for the long term and providing homes at social rents which deliver a social benefit for tenants and the government of around £20m a year - being the difference between lower market rents (Local Housing Allowance (LHA) level) and the rents charged by the Council to its tenants. This represents a saving of around £27 a week compared to the LHA. Within this income, service levels in terms of responsive and planned maintenance can be maintained and an element of replacement homes planned for. The Council in its partnership with Derby Homes has set aside resources to finance the building or acquisition of around 400 homes over the next four years within the HRA. Derby Homes will be additionally supplementing the HRA resource by setting aside funds to finance around a further 300 homes within existing planned fee levels. Contracts are already in place to deliver at least 60. This overall plan of up to 700 homes will be delivered by using a partnership approach to these issues, aiming to use the most appropriate means of delivery for each site and each service on a flexible basis.

The overall intention of the plan is to try to sustain social housing in a good condition and to continue to slowly modernise and refresh the stock appropriate to demand.

Background
Derby City Council still owns just over 13,000 Council homes, of which around a third are flats and two thirds houses. Almost half of the stock is of 3 bed houses – almost 6,000 of these remain, with the rest roughly 50% each of one and two bed homes.

These are managed and maintained by Derby Homes as agents for the Council. Derby Homes has also started to generate a small stock of its own through partnerships with the HCA and opportunities in the market, but the vast majority of Council owned stock remains directly owned by the Council.

Asset Management – Maintenance
The Council and Derby Homes consulted tenants in 2011 with a view to setting long term asset replacement cycles. These are now established and are working well to date. The core services have now reached a ‘minimum’ level following the massive effort and investment during Homes Pride (2002-6) which saw over £100m spent on improving Kitchens, Bathrooms, Heating systems and double glazing. Further investment has followed in Solar Panels (£6m in 2011) and in insulation of homes part funded by Community Energy Saving Programme (CESP) funding. Further significant investment in insulation is planned through the new Energy Company Obligations (ECO), probably in 2014. In addition, further investment in new doors and some roofing and electrical works are planned for 2014. There will be a significant increase in required spending from around 2022 onwards as kitchens and bathrooms replaced in Homes Pride again come up for renewal. As a result, it is critical that the HRA builds sufficient resources adequate to deal with that future requirement of the stock. Lower spending now cannot be sustained for ever, but helps hugely with the plan to invest heavily in about a decade’s time.

The overall Asset Management Strategy is being reconsidered as it should be periodically and any changes to it will be brought forward over the next year or so.

Asset Management – Development
The plan currently is to develop around 400 homes within the HRA over 3 or 4 years and then for a constant supply of around half of those lost through the Right to Buy (RTB) – estimated at around 50 to 60 a year.

The Right to Buy risk is set to increase further with a combination of legislative pressure – the proposed reduction in the qualifying period from 5 to 3 years – and the lack of being able to borrow the balance to replace as a result of the debt cap, plus the general economics that large discounts and higher rents encourage some tenants to consider buying their home from us. The ability to reinvest proceeds remains welcome but will only enable a limited scale of reinvestment as a result of the debt cap. Alternative, more sensible constraints on debts could be considered in order to ensure that debts do not become excessive, but a cash cap frozen at 2012 levels means a real terms reduction in borrowing capacity for Council housing. In order to increase overall capacity and to make sensible investments in flats without a Right to Buy, the plans allow for new flats to be delivered by Derby Homes and for new houses to be provided direct by the Council.

In order to fund the revenue losses incurred in the early years, Derby Homes will need to undertake significant cost savings to generate the funds required to subsidise those flats. The approach proposed is that Derby Homes continues to make efficiency gains including through joining up services with the Council and these savings are then reinvested into subsidising additional homes.

Demand is currently greatest for one and two bed properties, and this is where the majority of development effort will go, although a few larger properties will be considered to keep an appropriate balance.

Maintenance
Decent Homes standards will be maintained for the future through the approach already underway for major repairs, which will be consistently applied across the years. Day to Day maintenance standards have improved along with efficiency levels and the budget for this is likely to remain steady with additional service standards and improvements due to legislative change being largely absorbed by efficiency gains. Void levels have increased and if this continues may impact on the longer term plan, but is currently containable within existing overall resources.

Management
The Council has reduced the management fee to Derby Homes by £1m in real terms over 4 years, increasing the resources available overall for both maintenance and for replacement homes as a consequence. The business transformation programme that this required has its final year in 2014/15 and the final major saving has been delivered by the move of Derby Homes' headquarters into the new Council House.

Rent Levels
The government has made it clear that there will be further restraint on rent levels from 2015/16 onwards. Such restraint will place an additional burden on the HRA business plan over the longer term as income that would have been raised through rents will no longer be received. The intention appears to be to restrict individual rents to CPI (inflation) plus 1% in any one year. The rent increase for 2014/15 therefore appears to be the last one before this restriction is imposed. The existing plan is based on rents gradually reaching rent convergence with Target rent over the long term but mostly over the next two years. To continue with that policy would lose rental income of around £1.3m a year. This would have an impact on the scale of replacement homes that could be built or acquired. Depending on the final details of the proposals from the government, it may be possible to increase rents sufficiently in 2014/15 to reduce the rental losses to lower levels of perhaps £0.2m. This plan

assumes for planning purposes that the rental increase might be RPI+0.5%+£4 (2 years of £2) in 2014/15 and thereafter by CPI+1%. Final details of government rental policy are required before a final decision can be made.

Other detailed proposals for change to last year's plan
The Supported Living Service (SLS) for more vulnerable tenants used to receive Supporting People funding which is no longer available. As a consequence there was an initial shortfall in funding of around £0.8m which has been reduced by gradual means to currently £0.5m. It is expected that the proposed restructuring and integration of this team into wider housing management will go ahead. If this is approved by Cabinet, the HRA would fund part (£0.2m) of this new service, with Derby Homes meeting the rest. As a consequence, Derby Homes' management fee would then be increased by this amount but would in effect face an additional pressure to deliver further real terms savings to deal with the balance.

It is also proposed that Derby Homes' fee be increased by £80,000 with responsibility for grounds maintenance of HRA land being met from that funding.

The Estates Pride Programme is now established at an underlying £0.5m a year. Within this, it is suggested that the Crime Prevention Team which was previously funded by the old EP programme should continue to be funded at £50k a year, to match fund the same amount coming from Neighbourhood Management budgets.

The management fee for Derby Homes be reduced in real terms by £0.25m as planned, plus an adjustment for the loss of stock during 12/13 of £88k across management and maintenance.