Communities and Housing Scrutiny Committee – 21 January 2019

HOUSING REVENUE ACCOUNT (HRA) BUDGET AND RENT LEVELS FOR 2019/20

Joint Report of the Corporate Director, Place Management and Regeneration and the Borough Treasurer

1 INTRODUCTION

1.1 The purpose of this report is to provide the Scrutiny Committee with the opportunity to comment on an illustrative Housing Revenue Account (HRA) Budget. The Cabinet will be meeting on 5 February to recommend to Council an HRA budget for 2019/20, including the level of rent and service charges. The illustrative budget is based on a number of key assumptions set out in the report regarding income from rent and service charges; expenditure commitments contained within the HRA 30 year Business Plan and Asset Management Strategy and indicative spending requirements to support inflationary pressures and identified investment priorities.

1.2 This report takes account of the HRA Rent Strategy 2012 – 2017 which was approved by the Executive on 7 January 2013 and changes by the Department for Communities and Local Government with regard rents for social housing from 2016/17.

2 SELF FINANCING AND RENT LEVELS

2.1 As members are aware a new system for Council Housing Finance, Self Financing, was introduced for 2012/13. This replaced the system which was based on a national subsidy system.

2.2 The Self Financing offer from Government was based on a Government valuation of the Stockport HRA. This was calculated by estimating how much borrowing could be sustained by the HRA under the new finance system, based on Government assumptions on the amounts of income and expenditure to be received / borne by the HRA over the next 30 years.

2.3 In February 2012 the Executive agreed a 30 year Asset Management Strategy and Business Plan which provide for a longer term planning framework within which the rent levels and HRA budget for 2019/20 need to be agreed.

2.4 Since the implementation of Self Financing there have been two policy changes regarding rent policy:

1. Announcements included with the Budget for 2013 and the spending round for 2013 included changes to rent policy. A new rent policy for social rents was announced for a ten year period from 2015/16. The new policy is that from April 2015 rents in the social sector would increase by Consumer Price Index (CPI) inflation (as at September in the preceding year) + 1% annually. Previously, rents could increase by up to Retail Price Index (RPI) Inflation (as

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at September in the preceding year) + 0.5%, plus up to an additional £2 where the rent was below the formula rent for the property;

2. The summer budget of 2015 superceded the above and announced that the government will reduce rents paid by tenants in social housing in England by 1% a year for 4 years from 2016.

2.5 The first policy change resulted in the ending of rent restructuring a year earlier than the HRA business Plan as well as a rent increase being linked to the CPI rate rather than the RPI rate.

2.6 The second policy change altered funding assumed within the HRA Business Plan again. Rent increases in the Business Plan were assumed to increase by 2.5% per annum. Rental income is therefore lower than that set out in the original plan and further and ongoing efficiencies will need to be sought as a result of these changes.

2.7 In October 2017 the Government announced a return to CPI + 1% for five years from 2020/21 to 2025/26. This announcement is welcomed on the basis that it provides for more certainty to aid future planning and that it recognises that HRA business plans and the investment requirements to maintain the existing housing stock were predicated on future rent increases.

2.8 The CPI rate as at September 2018 was 2.4%.

2.9 It is important to note that the Business Plan was indicative and contained assumptions regarding both income and expenditure. The effects of the rent reduction have been modelled and while the HRA remains viable in the short-medium term it will face significant financial challenges compared to the original assumptions within the self-financing settlement as a result of:

- Cessation of rent convergence;
- Social Rents increasing by CPI rather than RPI;
- Social Rent reduction of 1% per annum for the four years beginning in 2016/17;
- Changes in Right to Buy discounts; and,
- Wider Welfare Reform Implications.

2.10 The HRA commences this period in a strong position due to the continued excellent management and performance. Stockport Homes continue to top perform in maximising rent collection and reducing void periods of properties. It should also be noted that other costs within the HRA Business Plan, such as interest on debt, are lower than that assumed in the original Business Plan. The future sustainability of the HRA will be reliant on the following areas:

- Ongoing over/top performance of financial targets by Stockport Homes;
- Effective treasury management by the Council and resultant interest rate gains;
- Efficient procurement and delivery of the capital programme of works by Stockport Homes including the prioritisation and optimal programming of works;
- On-going programme of Management Fee efficiencies;
- Continuation of invest to save projects; and
- Alignment between the HRA and general fund services in delivery of locality services.

2.11 The Cabinet Member for Communities and Housing has directed that a new Rent Strategy is developed over the coming months to report back to Scrutiny Committee and Cabinet in early summer that sets out proposals for rent levels in the context of the cessation of rent reduction directives from 2020/21, the need to maintain our decent homes standards, impact on tenants and the pressures facing the HRA following the reduction in rents by 1% for each of the last four years.

2.12 Limit rent is the maximum rent for rent rebate subsidy purposes, i.e. the maximum that would be covered by benefits towards housing costs. Following the further 1% rent reduction in April, average rents, at £72.77 will be £0.93 below the rent limit of £73.70.

2.13 In terms of Right to Buys (RTBs) the original business plan assumed 20 RTBs per annum. As a result of changes to the discounts available the Council has seen an increase in the number of RTB sales. In 2013/14 there were 82 sales, 57 sales in both 2014/15 and 2015/16, 61 in 2016/17, 97 in 2017/18 and the forecast for 2018/19 is for 70 sales. The illustrated HRA budget takes account of these and a further forecast for 90 sales in 2019/20.

2.14 It should be noted that average Council rents in Stockport are still relatively low, Stockport has relatively high house prices, and the Council's social rent levels are less than half of those charged by private landlords.

2.15 It should also be noted that for rents in shared ownership properties (70 properties) the rent element will increase by RPI plus 0.5% (3.8%) as per the agreements in place with these tenants.

2.16 The illustrated reduction of 1.0% in rents is imposed and therefore consultation with Stockport Homes tenants via a SHL customer hub meeting on 20 November focused on the continuation of the Government's rent reduction policy to 2020 and what that would mean. Customers were informed that 2019/20 would be the final year of the four year 1% rent reduction and that the Government rent policy would allow social housing providers to raise rents by a maximum of CPI +1% from 2020. Over the four years social rents have decreased by £2.98 per week and affordable rent by £4.97 per week. If rents had increased with inflation over this period this would have equated to an increase of £7.83 per week more for social rents and £13.06 per week more for affordable rents than the 2019/20 rents. Service charges were also discussed with customers at this event, with the focus on the principle of only increasing charges for services in deficit, in order that these services were not subsidised from rents.

2.17 The customer hub meeting was openly advertised to all tenants and 30 customers registered from across the Borough to attend with actual attendances of 16. The customer views and officer responses are summarised as follows: to address concerns over future repairs, customers were assured that the ongoing rent reduction to 2020 would not impact on maintaining the decent homes standard; it was agreed that further consultation would be carried out prior to the Government's proposed return to allow rent increases from 2020; no objections were raised by customers to the approach to service charge setting; some concerns were raised regarding the need for service charge increases generally with explanations provided that clarified the funding deficit and need to reduce / remove the subsidy through rental income.

2.18 The Board of Stockport Homes has considered the impacts on the business plan of previous policy announcements, coupled with lost future revenue income of higher numbers of RTBs.

2.19 At the time of this report, approximately 66% of tenants are in receipt of benefits towards their housing costs (Housing Benefit or Universal Credit) and it is expected that this level of tenants in receipt of housing cost benefits will continue during 2019/20.

3. SERVICE CHARGES

3.1 Service charges were un-pooled, i.e. separated out from the basic weekly rents a number of years ago. Service Charges are costs for specific services provided to certain properties rather than all the housing stock. A housing authority cannot profit from the recharging of services, although the cost of services should be met by service charge income. Stockport Council endeavours to keep annual service charge increases to CPI + 1% where possible, but there are occasions where greater increases are required to address service charge deficits. Such instances are illustrated in section 3.6. It should be noted that most service charges attract housing benefit.

3.2 Over the course of the current year, detailed service charge reviews have been carried out by the Service Leads for all services. This allowed the expected financial position for each service to be reviewed and highlighted the changes which would be required in order to ensure that services are sustainable.

3.3 The general principle proposed and illustrated for service charges in 2019/20 is to freeze charges for services where charges are sufficient to meet costs and recommend an increase of CPI+1% for those where deficits are currently being incurred. This supports the principle that service costs should be met by service charges and should not be subsidised by the wider customer base who do not benefit from those services.

3.4 There are a number of exceptions to the proposal for increases of CPI+1% where the cost of providing the service far outweighs the income received and these exceptions are detailed in the following paragraphs.

3.5 Service charge specific business plans are in place to reduce the gap between cost and income from charges. This level of scrutiny over service charge costs is performed in detail within Stockport which adds to the financial viability of the HRA. Overall service charges are in deficit by approximately £0.611m; however cost reduction initiatives undertaken by Stockport Homes in the previous years has reduced this from approximately £1m. This mitigates tenants cross-subsidising those who do receive service charges. This cost reduction work has also enabled some areas to be identified where freezes on charges can be applied.

Exceptions to CPI + 1% increase

3.6 The issue of heating charges and electricity has been on-going for a number of years and previously the Council has sought to minimise the impact of large increases on tenants through phased increases in previous years. Significant work has been completed to date to increase the energy efficiency of the district heating systems including extensive capital works on energy efficiency programmes and replacement of current systems with bio-mass boilers. Stockport Homes secured CESP and ECO programmes which attracted inward investment in excess of £14m to roll out large scale biomass heating across the Borough. Energy services are provided by external companies and cost increases in the wider external market result in a direct increase in the charges levied on private tenants and homeowners. Price increases in the energy market have been widely reported in the national press with OFGEM reporting that wholesale costs are 35% higher than a year ago. Stockport Council is similarly affected by these external market forces, and whilst it ensures that it receives the best prices for these services, cannot control a general market cost increase. An increase in energy service charges above CPI + 1% is recommended to ensure that Stockport Councils HRA account remains sustainable.

3.7 Heating energy prices are expected to rise by 23% over the coming year and a service charge increase of 10% is being proposed which will result in the service being in a balanced position. This would only apply to those sites in deficit and the application of this proposal would result in the following changes to customers:

Individual Heating – Non HB

Increase in £ per week	Number of customers affected
£0.51 - £1.00	844
£1.01 - £1.50	620
£1.51 - £2.10	38

3.8 Similar to heating, wholescale electricity energy costs are increasing and a 13% increase in cost is expected for 2019/20. Again increases will only apply to sites in deficit and it also proposed that no tenant will receive an increase of more than £1 per week. This service is eligible for Housing Support. Applying the proposed increases would result in the following changes to customers:

Communal Electricity

Increase in £ per week	Number of customers affected
£0 - £0.25	1,863
£0.26 - £0.50	2,584
£0.51 - £0.75	88
£0.76 - £1.00	85

3.9 The review of the communal TV aerials service highlighted the substantial investment works taking place to upgrade the existing systems however also demonstrated that the ongoing maintenance costs are not met through the existing service charges. It is proposed to increase the service charge by 9p per week for 1,789 customers. This service is eligible for Housing Support.

3.10 Finally the review of the communal laundry services highlighted that the costs of providing the service are not met through the current service charges and that the charge is far less than customers would pay to use commercial facilities. The proposal is to increase the charge to £4.50 per week which is an increase of between £1.64 and £2.30 per week for 321 customers. This service eligible for Housing Support.

3.11 A full review of caretaking charges was undertaken in 2015 and it is proposed that there is a cap of £12 per week at Lancashire Hill implemented in April 2016 is continued into 2019/20.

3.12 For Housing Benefit eligible customers the maximum increase would be £2.10 per week (relating to individual heating). For non-Housing Support eligible customers the impact would be dependent on the services received. These are set out below and include all other service charges a single line worst case scenario together with a total worst case scenario where customers are in receipt of all services referred to. The table also includes an assessment of the actual net increase taking into account that rents are reducing, which is on average a £0.73 per week reduction, and if an inflation only increase were implemented in these service charges which would equate to £1.74.

SERVICE	COST	Net Cost**
Heating	£2.10	-£0.37
Communal Electric	£1.00	-£1.47
TV aerial	£0.09	-£2.38
Laundry	£2.30	-£0.17
All other services	£1.34	-£1.13
ALL SERVICES (worst case)	£6.83	£4.36

** This is an illustration taking into account the average rent decrease coupled with the rate of inflation that has occurred

4 HRA BUDGET 2019/20

4.1 An illustration of the budget for the HRA for 2019/20 is set out in Appendix 1. It illustrates the rent reduction of 1.0% and other charges are increased as set out in section three. The illustrative budget provides for a level of balances of £1m which is viewed by the Borough Treasurer to be the minimum considered necessary to support the illustrated HRA budget. This is based on an initial assessment of risk and the robustness of the estimates as detailed in the calculations contained at Appendix 2. Should any substantial changes be made to the illustrative budget a further risk assessment would have to be undertaken.

4.2 There are some key budget lines within the HRA that through extensive performance management have improved the revenue position within the HRA year on year, and have enabled the HRA to face the challenges ahead in the best possible position. Whereas lines such as external interest rates are harder to influence, the management of the stock is key to ensuring the on-going viability of the HRA. The management by Stockport Homes of void and rent collection has resulted in significant extra resources for services to tenants based on improved collection levels and much reduced void loss. Coupled with the management of procurement efficiencies via the Capital Programme, which has resulted in significant levels of savings, the HRA remains in a strong position to continue to deliver quality services and stock investment to tenants while facing the financial challenges ahead. It is important that the performance management in these key areas continues to be maximised if the HRA is to operate at optimum efficiency.

4.3 While the Stockport HRA remains robust it is clear that the 1% rent reduction has had impact and while noting the benefit to tenants the future cost pressures on delivering services and maintaining decent homes will need to be taken into consideration as part of the future rent strategy to be developed as detailed earlier in the report,

4.4 The management fee paid to Stockport Homes will see an overall cash increase of £0.473m which includes increases to reflect the recurrent nature of previous agreed delivery plan initiatives, recognition of pay and inflationary pressures and delivery of a 3% efficiency.

4.5 Stockport Homes continues to maintain a focus on delivering value for money to ensure that efficiencies are released and services to customers are not adversely impacted and the best possible outcomes for customers are delivered within the resources available. The commitment to maximise the impact of the resources available are documented and demonstrated through Stockport Homes' continuous improvement framework, delivery plan, the HRA business plan and the value for money strategy.

4.6 The main features of the illustrated spending plan for the HRA are as follows:

- The Stockport Homes Management fee reflects the delivery of 3% efficiencies, inflation expected on repairs and maintenance expenditure and the cost of the anticipated pay award, currently budgeted at 2% and the mainstreaming of services agreed via the delivery plan process;

- After allowing for the above commitments the HRA budget would have a in year deficit of £0.578m following an appropriation of reserves of £0.250m. This deficit together with one-off brought forward resources of £0.615m allows for further non recurrent investment of £0.037m during the year. This will fund some temporary universal credit admin support and an upgrade to the systems for processing RTBs.

4.7 While resources are available for investment in 2019/20 the long term viability of the HRA needs careful consideration as investment requirements increase over the life of the asset management strategy as does ambitions for new build.

4.8 The capital programme for the HRA in 2019/20 and future years, based on the illustrative budget would be as follows:

Table Two – Illustrated HRA Capital programme 2019/20 – 2020/21

	2019/20 £000s	2020/2021 £000s
HRA Capital programme		
General Capital Programme	17,121	14,588
New Build programme	1,538	0
Total HRA Capital Programme	**18,659**	**14,588**
Funded By:		
Grants / Other receipts	456	0
Directly Funded Borrowing	6,155	2,334
RCCO – including depreciation charge	11,898	12,254
HRA Capital Reserves	150	0
Total Funding for Capital Programme	**18,659**	**14,588**

4.9 The HRA capital programme for 2019/20 – 2020/21 is in line with the HRA Asset Management Strategy and also takes account of the new build programme within the Housing Revenue Account.

Sprinkler investment options

4.10 Following on from the Grenfell disaster, the installation of sprinkler systems has been deemed a strategic priority by the Cabinet Member for Communities and Housing. There are three options for how this could be funded:

4.11 Option One – The cost of the sprinklers are included within the capital programme and are absorbed within the existing budgeted resources. The total estimated cost for sprinklers is £9m with a further £1m for remedial works. This obviously would impact on current projects within the programme.

4.12 Option Two – The HRA borrows additional resources for the total cost. This would be modelled and budgeted for accordingly to ensure adequate funding for the total capital programme is available.

4.13 Option Three – is a hybrid approach of the above two options, i.e. do some of the cost in the current programme, some is borrowed.

4.14 All options are ultimately deliverable in the absence of a debt cap, however borrowing incurs additional cost and it needs to be clear how this will ultimately be funded. These options will be considered as part of the Capital Programme Budget for 2019/20 and it is recommended that option 3 is developed, implemented and reported back to Scrutiny Committee and Cabinet.

4.15 It is noted that development within the HRA is just one aspect of the Council's commitment to build new affordable and shared ownership homes within the borough. The cessation of the debt cap allows for more provision for new build options within the HRA in the future. Through the loan facility provided to Stockport Homes the current on site developments are expected to deliver 147 new homes during the year with a further 364 within the existing pipeline of developments.

4.16 The above illustration indicates a requirement for additional borrowing of £6.155m in 2019/20 which would be sustained from resources within the HRA. During 2018 the government have implemented the abolishment of the debt cap.

4.17 The 2019/20 year is a 53 week year. This is causing some issues in the sector as the Department for Works and Pensions do not recognise a week 53 for Universal Credit payments. This would leave a claimant short of money for one week and landlord issues would be experienced in increases to arrears. Local Government and the Housing Sector have raised this issue with the Department and Scrutiny Committee and Cabinet will be informed of any developments.

4.18 Based on the illustrations contained within the report total balances expected to be held within the HRA would be £1m in 2019/20 as per paragraph 4.1.

5 RECOMMENDATION

The Scrutiny Committee is asked to comment on the report and the illustrative HRA Budget for 2019/20.

BACKGROUND PAPERS

There are none

Anyone wishing to inspect the above background papers or requiring further information should contact Michael Cullen on Tel: 0161 474 4631 or by email on michael.cullen@stockport.gov.uk

Appendix 1

Illustrative Housing Revenue Account 2019/2020

Expenditure	Budget 2018/19 £000	Forecast 2018/19 £000	Illustrative Budget 2019/20 £000
Management Fee	27,794	27,794	28,267
Council HRA Costs	1,362	1,362	1,362
Rents, rates, taxes & other charges	180	180	180
Total management & maintenance	**29,336**	**29,336**	**29,809**
HRA share of interest charges (Per Item 8 Debit)	5,089	5,017	5,139
Depreciation of fixed assets	10,893	11,551	11,898
Debt management costs (Treasury Management)	65	65	65
New Build MRP, Interest and other	1,109	1,080	1,104
Bad debts provision	400	380	510
Solar PV Interest	124	123	123
Solar PV Voluntary MRP	126	0	0
Future Development Provision	262	242	239
Water Charges	4,815	4,812	4,981
	22,883	23,270	24,059
Total expenditure	**52,219**	**52,606**	**53,868**
Income			
Rents of dwellings	(43,030)	(42,889)	(42,156)
Rents (non dwellings) shops/garages/office rents	(300)	(300)	(300)
Charges for services & facilities	(3,537)	(3,517)	(3,856)
Solar PV FIT Income	(1,300)	(1,300)	(1,200)
Renewable Heat Incentive	(415)	(247)	(395)
Appropriations / Retained Income from RTBs	(117)	(91)	(117)
Water Charge Debit	(4,815)	(4,812)	(4,981)
Total	**(53,515)**	**(53,156)**	**(53,005)**
Net cost of services	**(1,296)**	**(550)**	**863**
Net cost of premia less discounts	(5)	(5)	(5)
Investment income	(70)	(30)	(30)
	(75)	**(35)**	**(35)**
Net operating expenditure	**(1,371)**	**(585)**	**828**
Capital met from revenue – Business Plan	1,315	0	0
Voluntary MRP	0	0	0
Contribution from Reserves	0	0	(250)
(Surplus)/Deficit for year	**(56)**	**(585)**	**578**
(Surplus)/Deficit brought forward - HRA	**(1,123)**	**(1,104)**	**(1,615)**
Additional RCCO	**0**	**0**	**0**
Future investment reserve	**179**	**74**	**37**
Accumulated (surplus)/deficit at year end	**(1,000)**	**(1,615)**	**(1,000)**

Appendix 2

2019/20 Illustrative Housing Revenue Account Budget - Risk Assessment

Item	Budget Assumption £000s/%	Possible Variance from Assumption £000s/%	Impact Cost/ (Benefit) £000s
Previous Financial Year			
20% Variance between budget & forecast outturn for 2018/19	0	20%	0
Pay & Prices			
N/A – contained within management fee payable to Stockport Homes Limited			
Income			
Yield from Rental and Service Charge Income	46,312	1.5%	695
Void Rate	0.75%	0.25%	115
Investment Income	30	0%	0
Interest rates / other changes			
Interest and other expenditure (excluding Water charges)	19,078	1%	190
Minimum Level of HRA Balances			**1,000**

Risk Assessment Methodology & Commentary

1 Although the estimates contained in this report are based upon the best available information at the time of writing, it is important to recognise that a degree of uncertainty surrounds them. Estimates are prepared on the basis of judgements about what is thought to be the most likely outcome for a series of key events which are relevant to the budget.

2 The key assumptions underpinning the estimates in this report are based on the most likely outcome for a series of key events. The above risk assessment takes those key assumptions and calculates the financial impact of possible variations.

3 The risk assessment is therefore a 'sensitivity analysis' showing the financial impact of possible variations to key budget assumptions. The figure that is calculated is then used as the basis for a recommendation regarding the minimum level of general balances.

4 The key risks reflected in the above assessment include:

- Uncertainty regarding actual rates of interest, and yield from rental and service charge income; and,
- Potential for void rates to be higher at 1.00% than the 0.75% included within the financial assumptions.