NORTH WEST LEICESTERSHIRE DISTRICT COUNCIL

CABINET– 29 JULY 2014

Title of report	**UPDATING THE HOUSING REVENUE ACCOUNT BUSINESS PLAN**
Key Decision	a) Financial Yes b) Community Yes
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Purpose of report	To provide information for the Cabinet to take into account when considering the report on the agenda on funding for the Decent Homes Programme
Reason for Decision	The information provided in this report will influence the Cabinet's recommendations to Council for funding to complete the Decent Homes Programme.
Council Priorities	Value for Money Homes and Communities
Implications:	
Financial/Staff	The implications of the decision are covered in the report
Link to relevant CAT	Not applicable
Risk Management	The risks associated with the decision are covered in the report
Equalities Impact Assessment	The implications of the decision are covered in the report

Human Rights	Not applicable
Transformational Government	Not applicable
Comments of Deputy Chief Executive	The report is satisfactory
Comments of Section 151 Officer	The report is satisfactory
Comments of Monitoring Officer	On the advice of Bevan Brittan this report is satisfactory
Consultees	Housing Revenue Account Business Plan Project Board
Background papers	**Additional Costs of the Decent Homes Improvement Programme 2014/15 (Cabinet - 4 March 2014)** **Call-in of Cabinet decision of 4 March 2014 entitled 'Additional Costs of the Decent Homes Programme 2014/15' (Policy Development Group - 12 March 2014)**
Recommendations	**THAT CABINET NOTE THE CONTENTS OF THIS REPORT IN THE CONTEXT OF CONSIDERING THE REQUEST FOR ADDITIONAL FUNDING FOR THE 2014/15 DECENT HOMES PROGRAMME AS DETAILED ON THIS MEETING AGENDA**

1.0 BACKGROUND

1.1 This report is linked to the item on the agenda for this meeting entitled "Additional Costs for the Decent Homes Improvement Programme 2014/15".

1.2 The Housing Revenue Account Business Plan was originally approved by Cabinet on 27 March 2012, and provides the service and financial planning framework for the delivery of the Council's landlord services over a 30 year period. The Business Plan has two key elements, the narrative text section, and a financial spreadsheet model, which forecasts income and expenditure levels over the full 30 year plan period.

1.3 When the Business Plan was originally established it was proposed that it would be updated annually to reflect actual expenditure in the previous year and any budget adjustments, and fully reviewed every 5 years. However, in response to the additional funding required to deliver the Decent Homes Improvement Programme (DHIP) in 2014/15 and a range of other changes that have affected the Plan's base assumptions, it is being reviewed earlier than originally planned, as part of the preparations for the 2015/16 budget setting process. Cabinet will be asked to approve the revised HRA Business Plan, as part of the 2015/16 budget setting process.

1.4 This report provides Cabinet with an introduction to the key issues being addressed in the reviewed business plan, and illustrates how they interlink with the additional funding required to complete the 2014/15 improvement programme.

2.0 THE BUSINESS PLAN FINANCIAL MODEL

2.1 The HRA Business Plan financial model covers a 30 year period and illustrates income and expenditure projections over the plan period. As part of the review being completed the plan is being rebased, with 2014/15 as year 1 of the 30 year cash flow model. In addition to this, we have also introduced a revised and updated spreadsheet model from our business planning professional advisors the Chartered Institute of Housing (CIH), which incorporates all current housing finance legislation. The new baseline plan uses information from the provisional outturn figures for the HRA and the Capital programme for 2013/14. Both of these are subject to confirmation by members as part of the outturn approval process over the coming months, and any amendments made as part of this process will require the business plan model to be adjusted accordingly. It also incorporates the revised HRA and Capital Programme budgets approved by Council on 25 March 2014.

2.2 Part of the process of reviewing and updating the plan includes the following mandatory updates to reflect current position:

- Updated balances for the Housing Revenue Account (HRA) and Major Repairs Reserve (MRR).

- Revised 'Year 1' income and expenditure to reflect 2014/15 budget.

- Revised housing stock numbers to reflect the number of properties within the rental system available for let following deduction of previous years' right to buy sales and decommissioned sheltered schemes.

- Updated the opening debt to reflect the partial repayment of annuity loans.

2.3 In addition, the following revisions have been made to enable more accurate forecasting of future cash flows:

- The number of assumed Right to Buy (RTB) sales in the future has been increased to reflect the more recent trends since the Government increased the discounts available to tenants.

- The vacant property percentage rate used in the model has been increased from 0.75% to 1.09% (£184k) for 2014/15 and 1.8% from 2015/16 (£319k) to reflect current position. This will be kept under review and adjusted back down as vacant property numbers reduce once the improvement programme is completed. The original level of vacant properties is still considered to be the typical level we will experience over the medium to long term. Completing the decent homes improvement programme has resulted in a number of properties remaining empty for longer than normal as a result of the need to coordinate different contractors completing different works in them. This situation has been compounded by an increase in the number of properties coming vacant, which we believe to be only a short term situation.

- The provision for bad debt been has increased from 0.4% to 1% (to £169k). This reflects the increase in bad debt provision approved as part of the 2013/14 budget setting process in preparation for anticipated higher levels of debt following the introduction of Welfare Reform.

- The Rent Convergence date for converging property rents has been amended from 2015/16 National Government Policy target date to 2016/17 which is the date that the majority of properties will meet convergence (although his will require further amendment in the light of the recent Government announcement on future rent policy also referred to in this report).

- Revenue Contribution to Capital Outlay (RCCO) provision has been amended in the model to be input at a pre-determined level for 2014/15 rather than calculated amount.

2.4 The rebased 2014/15 model shows a healthy long term future for the Council's landlord activities based on current assumptions and current social rent policy. A previously known projected funding shortfall issue presents itself in year 8 of the plan (2021/22), with a need to source additional resources of £112k. This is because we have to repay two of the maturity loans of £10 million and £3 million fall due for repayment. Options to fund this shortfall will be considered once the final amount is confirmed as part of the ongoing budget setting process, and could include reductions in revenue expenditure, or simply refinancing the loans. The amount required is a significant reduction from the previously forecast sum which was in excess of £1m. The reduction is as a result of the incorporation of projected under spending from the 2013/14 capital programme into the model, and other changes as a result of amendments to the assumptions the model is based on, as detailed in this report.

2.5 The baseline 2014/15 model excludes the additional estimated £3.063m required to fund additional non decent properties. Financial modelling of the options available to fund the improvements has been undertaken and is detailed under Section 4.

2.6 The revised baseline model future capital funding projections remain based on information derived from our previous housing stock condition information. The new stock condition surveys of all homes, completed over the last three years as part of the decent homes programme are currently being analysed to allow us to revise our future funding projections, and this information will be built into the business planning process for consideration as part of the 2015/16 budget setting process.

3.0 THE BASELINE BUSINESS PLAN FINANCIAL ASSUMPTIONS

3.1 As part of the process of reviewing the business plan, there are a number of areas that require updating and revision to reflect the current position. This section of the report explains the proposed areas we will be reviewing.

3.2 The general inflation rate contained in the financial model has not been revised and remains at 2.5%, and therefore all classes of income and expenditure increase by this amount (unless singularly varied and referenced below):

3.3 Depreciation has been amended in the model to actual 2014/15 figure. In addition the model has been amended so that the value is not increased by the general inflation rate as this represents the advice we have received from Charter Institute of Housing.

3.4 The forecast level of Retail Price Index (RPI) which currently drives the annual rent increase also remains at 2.5%, with the formula rent increase percentage remaining at 0.5% to reflect current national rent policy. Details regarding the potential impact of proposed changes to rent policy are detailed in section 3.6 of this report.

3.5 Decent Homes Improvement Programme - additional costs have been identified relating to the delivery of the 2014/15 improvement programme, as previously reported, and falling into three categories -

A. Additional improvement works costs - £1,650,058
B. Funding for newly identified non decent homes - £2,444,270
C. Funding for non grant eligible non decent homes - £618,895

The funding required to address item A has been identified and approved by Cabinet/Council with consequent amendments being made to the approved budget for 2014/15.

The proposed source of funding for items B and C has also been identified as explained in a separate report on this agenda.

As part of the evaluation of the options to provide this additional funding, an assessment of the impact of additional borrowing on different terms was completed. Following this review, it was decided not to recommend additional borrowing as a source of funding for the additional costs, as the required funding could be obtained from existing sources within the capital programme and HRA balances, thus avoiding any interest charges which would be associated with any loan funding.

3.6 Future Government Rent Policy – as part of the introduction of the HRA self financing regime, the Government retained control of national social rent policy. This was to allow control of Housing Benefit expenditure and to seek to retain the alignment between Housing Association and Council rent levels which was being achieved through the rent restructuring process.

In October 2013 the Department for Communities and Local Government (DCLG) consulted all social housing providers on proposed amendments to social housing rent policy. The proposed changes include an amendment to the formula used for increasing rents, replacing the Retail Price Index (RPI) + 0.5% with Consumer Price Index (CPI) + 1%. Over time it is anticipated that this will produce lower rent increases for tenants, however it also reduces the level of income from rents within the business plan. If rental income increases at a slower rate than costs increase, this will create pressures within the business plan, which will need to be managed carefully.

Also included in the proposed changes is the removal of 'rent convergence', a system by which rents that are at a lower level are increased by a further up to £2 per year until they reach what is called limit rent or target rent. The current proposal is that all rents will be increased by the new formula only from their position at April 2015 and there will be no additional increases for those whose rent is not already at the 'limit rent' level.

DCLG announced the outcome of their consultation and confirmed the new Social Rent policy in June 2014.

Initial assessment of the impact of both of these changes has been modelled in a version of the HRA Business Plan 30 year cash flow model. When compared to the current Baseline version of the plan, the resultant loss in income over the 10 year period from 2014/15 to 2023/24 could be up to approximately £15m. Detailed work on the changes and flexibility granted by DCLG and resulting impact to the HRA is currently being undertaken and Members will be advised of any changes to the business plan we consider are necessary during the 2015/16 budget setting process.

3.7 Right to Buy - the level of council house sales has increased in recent years as shown in the table below, and it is assumed that the recent announcement that the Government will be appointing "Right to Buy Agents" to promote the scheme nationally will further stimulate interest from tenants in purchasing their homes.

Year	**2011/12**	**2012/13**	**2013/14**
Number of Sales	2	15	36

The increased level of sales has been factored into the revised business plan, and both income (due to reduced rent paid) and expenditure (due to fewer properties to repair and improve) are being adjusted accordingly.

In June 2012 we signed an agreement to retain all of the receipts we received from right to buy sales over and above an agreed level as part of the Governments one for one replacement initiative. Under the present arrangements the income from right to buy sales is split between the Council (25%) and the Government (75%). The new arrangements mean that we can retain all of the surplus receipts above an agreed level, on condition that we add to them from our own resources, and reinvest them in providing additional affordable housing within a given timeframe.

The formula through which we assess whether we have qualified to retain receipts is complex and can only be implemented each quarter after property sale numbers and values are confirmed.

Right to buy sales in Quarter 4 of 2013/14 represented a level where we qualified to retain receipts under the one for one replacement provisions, with £122,178.35 retained. Under the agreement we are required to supplement this to raise the available resources to a total £407,261.17 which is to be spent on providing additional rented homes by 31 August 2017. The funding for this will be incorporated into the 2015/16 capital programme.

There are a number of options available for the Council to fulfil its one for one replacement obligations, these include:

- Partnership working with a Registered Provider (RP) by providing grant funding to develop affordable homes.
- Partnership working with a RP by using them as developing agent.
- The Council directly deliver the replacement affordable home programme.
- Special Purchase Vehicle

- Buy Back (repurchase of former Council properties sold under the Right to Buy).
- Purchasing existing or new properties from developers of private owners.

These options are currently being evaluated and recommendations regarding the proposed approach to delivering the required additional properties will form part of the 2015/16 budget setting process.

3.8 Garages and Hard Standings - the Council has 383 garages and 240 sites (hard standings) which are available to let to local residents. The potential annual income from rental charges is £158,968, however only 51% (£80,686) is being achieved due to the location and/or condition of many of the sites and garages.

Following a review of the garages and hard standings it is proposed that a Garages policy be adopted, which is due to be considered by Cabinet in the summer of 2014. This will provide the policy position from which we intend to develop a 10 year garage site improvement programme, and consider some sites for redevelopment where appropriate.

3.9 Review of Sheltered Housing Schemes - Cabinet approved the decommissioning of three sheltered housing schemes in September 2011 with two further schemes identified as not having a long term viable future. One scheme has been disposed of on the open market achieving a capital receipt of £325k. The options for the future use of the buildings other buildings is currently being finalised and will be addressed as part of the 2015/16 budget setting process.

3.10 Empty Properties - As at 7 April 2014, there were 250 empty properties of which 64 are in the sheltered schemes referred to above. These, and a further 65 properties are 'out of debit' which means they are effectively removed from our stock numbers along with the associated rental income. Decisions to undertake intrusive asbestos surveys and Decent Homes improvements whilst the properties are empty together with the level of empty properties being higher than anticipated has resulted in reduced rental income of £333,811 which equates to 2.04% of the gross rental income for 2013/14, and this has been factored into our revised business plan.

3.11 Post 2014/15 improvement programme priorities – as part of the detailed preparations for the 2015/16 budget setting process, the level of funding required to sustain all tenants homes at the decent homes standard after 2014/15 is being re-evaluated. The outcome of this work could revise the level of funding required from 2015/16 onwards from the level currently projected in the business plan, which was based on 2006 stock condition information. The outcomes of this work will also impact upon the level of capital funding available for new initiatives, such as an accelerated improvement programme or new build, and is due to be completed in time to inform the 2015/16 budget setting process.

3.12 All of these factors are currently being incorporated into the revised HRA Business Plan, and the revised document will be considered for approval as part of the 2015/16 budget setting process.

4.0 FINANCIAL IMPLICATIONS OF ADDITIONAL COSTS OF THE DECENT HOMES IMPROVEMENT PROGRAMME ON THE HRA BUSINESS PLAN.

4.1 The detailed implications of the medium to long term impact of the proposed approach to funding the additional costs of the 2014/15 decent homes improvement programme have been evaluated. Financial modelling has been undertaken on financing the required funds through the use of HRA reserves and unallocated balances within the capital programme, to fund the estimated additional costs of £3.06m. This approach to securing the required funding is considered to represent better value for money to the Council than borrowing the funds, as interest charges are avoided, and investment income from balances held is currently very low.

4.2 The proposed approach to funding the additional £3.06m required to complete the decent homes programme in 2014/15 is detailed in the separate report to Cabinet and involves the use of the following sources of funding –

- **£613,451** 2014/15 Capital Programme, unallocated contingency.
- **£1,206,359** - Capital Programme, underspend from 2013/14 (subject to confirmation as part of the final accounts process)*.
- **£1,243,355** - HRA Balances, through an additional Revenue Contribution to Capital Outlay ("RCCO") (in addition to the £1,679,058 already included in the approved HRA and Capital Programme budgets for 2014/15).

*In the event that the 2014/15 Decent Homes expenditure is less than projected less will be needed to be taken from HRA balances.

The impact of this funding on the Business Plan will be to increase the size of the projected shortfall in year 8 of the plan (2021/22) from £112k to circa £3.3m.

The principle options to address this funding requirement are -

- Reducing ongoing revenue expenditure to create budget capacity. This option would require revenue savings of £471k per year for 7 years to generate the required £3.3m by 2021/22. Savings would not have to be made equally each year.
- Refinancing the loans rather than repaying them. There is an option to re-borrow the required funds, but this would be subject to future revenue costs for repayment and the interest rate for the loans cannot be projected with absolute accuracy.
- A combination of revenue reductions and refinancing.

Using reserves/balances would utilise existing HRA resources and as a result the Council would not incur any additional interest costs in borrowing additional funds. There would be a reduction in interest income on balances though, although given the low level of interest rates this is not projected to be more than £10k per annum.

The currently approved RCCO budget of £1.679m would increase by £1.243m to £2.922m.

Additionally it is important to note that the impact of changes in Government social rent policy recently announced have not yet been modelled, and we will also be updating our future investment requirements in response to the updated housing stock condition survey analysis currently being completed. Both of these factors will be addressed as part of the process of revising the business for the 2015/16 budget setting process.

5.0 CONCLUSION

5.1 This report is designed to advise the Cabinet of a range of issues relating to the HRA Business Plan which are currently being updated. This also reflects the current position following the identification of additional funding requirements to deliver the 2014/15 improvement programme.

5.2 The revised HRA Business Plan will be the subject of a report to a future Cabinet meeting as part of the preparations for the 2015/16 budget setting process.