REPORT TO:	**OVERVIEW AND SCRUTINY COMMITTEE**	**AGENDA ITEM: 6**
DATE OF MEETING:	**11 FEBRUARY 2015**	**CATEGORY: RECOMMENDED**
REPORT FROM:	**DIRECTOR OF FINANCE & CORPORATE SERVICES**	**OPEN**
MEMBERS' CONTACT POINT:	**KEVIN STACKHOUSE (01283 595811)** **Kevin.stackhouse@south-derbys.gov.uk**	**DOC:** u/ks/budget round 1516/base budget policy reports/6 HRA/budget report 15 16
SUBJECT:	**HOUSING REVENUE ACCOUNT BUDGET 2015/16 and PROPOSED RENT INCREASE**	**REF:**
WARD(S) AFFECTED:	**ALL**	**TERMS OF REFERENCE:**

1.0 Recommendations

1.1 That an average rent increase of 2.2% for tenanted properties is approved for 2015/16.

1.2 That the proposed estimates of income and expenditure for 2015/16 for the Housing Revenue Account are considered and referred to the Finance and Management Committee for approval.

1.3 That the updated financial projection on the HRA Business Plan as detailed in **Appendix 1** is approved.

2.0 Purpose of the Report

2.1 As part of the annual financial planning cycle, the report details the Housing Revenue Account's (HRA) base budget for 2015/16. The report also sets out details of the proposed rent increase for 2015/16 in accordance with the strategy approved in the HRA Business Plan.

3.0 Detail

3.1 During 2014, the Business Plan for the HRA was subject to a detailed review and update. This was to consider the resources available for New Build and to update the financial projection following the first 2 years of "self-financing" together with the impact of changes to the national rent setting guidelines, to be implemented in April 2015.

3.2 The Business Plan review was undertaken by a group consisting of members and tenants, supported by officers. The group reported in November 2014 and the revised business plan, comprising a 30-year financial projection, was considered and approved by the Committee in December 2014.

3.3 This report confirms the base budget resources for 2015/16, with updates where necessary, together with the proposal for a rent increase in 2015/16. This is in accordance with the Policy approved in the updated Business Plan.

Formulating the 2015/16 Base Budget

3.4 Many budgets have generally been calculated on an incremental basis, i.e. they are maintained at the same level as the previous year adjusted only for known changes and variations that have been identified through a restructure or efficiency programme. This approach is mainly applied to staffing costs.

3.5 However, many other budgets are subject to a base line review which is used to justify proposed spending. This process places greater responsibility on budget holders to justify their spending budgets by specifying their needs in a more constructed manner.

3.6 In addition to identifying possible budget savings, it can also identify potential cost pressures.

On-going Service Provision

3.7 The budgets are based substantively on a continuation of existing service provision (in respect of staffing levels, frequency, quality of service, etc.).

3.8 However, the full year effects of previous year's restructures and efficiencies are included, with any non-recurring items removed as identified in the report.

The Position entering the Budget Round

3.9 The Financial Plan, approved in December 2014, was based on updated spending information following the 2013/14 budget out-turn for the HRA, together with changes following the previous review in January 2014.

3.10 Various factors are modelled into the Plan with assumptions regarding future interest rates and inflation. In addition, the Plan was based on:

- The approved first phase of the New Build programme starting in 2014/15.
- Revisions to the staffing structure in Housing implemented in July 2014.
- Recent increases in right to buy sales.
- Base inflation for rent increases starting at 1.5% and rising to an average of 2.5% over the planning period.
- An assumed rent increase of 2.5% in 2015/16

- An increase in interest paid on the variable element of the "self- financing debt."

3.11 The Plan was fully costed over its 30 year life and showed a sustainable financial position whilst delivering the existing capital investment programme, repaying debt and delivering the 1st phase of the New Build Programme.

3.12 This was on the basis that the HRA's General Reserve would remain at a minimum level of £1m from year to year as set out in the Council's Financial Strategy.

Updated Budget 2015/16

3.13 Most of the assumptions and variables in the financial plan remain unchanged following the base budget review. There have been 3 main changes and these relate to:

- The proposed rent increase in 2015/16 – reducing from 2.5% to 2.2% (i***f approved***) due to a reduction in the base rate of inflation.

- The interest rate forecast on variable rate debt – reduced from 1.5% to 1.1% based on latest interest rates.

- The phasing of New Build – with the main projects currently approved commencing fully in 2015/16. The Business Plan had assumed that the New Build programme would commence in 2014/15. Although sites have been identified and a procurement exercise has been undertaken, actual works are not expected to start on site now until early in 2015/16.

3.14 Compared to the financial plan previously approved, this has increased estimated net expenditure in 2015/16 by £52,000. This has not materially affected the overall financial position in 2015/16.

Longer term Plan

3.15 The financial model is established and is designed so that a £1m minimum balance is maintained on the HRA's general reserve and that planned resources are set aside for debt repayment. These are the priority financial objectives to ensure that the Business Plan is sustainable.

3.16 Given that these two objectives are met, any increase or decrease in resources are reflected in the planned capital or new build programmes and these are flexed accordingly into the longer term. Effectively, the financial model is based on sustaining the core housing service.

3.17 Unless there is a significant change in resources in any year, this should not affect the short to medium term position. However, the cumulative effects of a change in one year, over 30-years, can affect the longer term aspirations built into the Plan.

3.18 The main focus of the Plan is over the medium term period of between 5 and 10 years. This ensures that any changes do not materially affect plans already in place to deliver the approved capital investment and new build programmes.

3.19 The updated 10 year projection is detailed in **Appendix 1**. A summary of the base budget for the HRA is shown in the following table.

HRA Base Budgets 2014/15 to 2015/16	**Approved Budget 2014/15 £'000**	**Proposed Budget 2015/16 £'000**	**Change £'000**
INCOME			
Rental Income	12,390	12,591	201
Void Losses	-81	-82	-1
Service Charges	140	140	0
Garage and Other Income	103	105	3
Grants & Recharges	284	284	0
Total Income	**12,835**	**13,038**	**203**
EXPENDITURE			
General Management	1,573	1,617	44
Supported Housing	839	756	-83
Bad Debt Provision	43	44	1
Responsive & Cyclical Repairs	3,287	3,395	108
Total Revenue Expenditure	**5,742**	**5,812**	**70**
Add : Interest/Capital Adjustments			
Interest Paid	1,599	1,685	86
Cost of Servicing Debt	275	8	-267
Interest Received from General Fund	-13	-16	-3
Depreciation	2,805	2,853	48
Total Expenditure	**10,408**	**10,342**	**-66**
Net Operating Income	**2,427**	**2,696**	**269**

3.20 The net operating income is transfererd to the Major Repairs Reserve which is the fund used for the capital investment programme. The provision for depreciation is also transfererd to this Fund.

3.21 The increase in rental income (subject to approval) assumes an average rent increase of 2.2% in 2015/16, adjusted for right to buy sales. The increase in responsive and cyclical repairs is in accordance with the main Business Plan and allows for inflation in the building cost index.

3.22 The cost of servicing debt in 2014/15 relates to the early termination payment on a fixed interest loan that was repaid on 2nd October 2014. This was reported to the Finance and Management Committee in December 2014. The subsequent savings on future interest payments of £48,000 per year were included in the Business Plan review.

HRA Reserves

3.23 The HRA has 3 separate reserves as follows:

Working Balance or General Reserve	Held as a contingency with a minimum balance of £1m.
New Build Reserve	Accumulated Capital Receipts pending expenditure on building new properties. The financial model assumes that these are drawn down each year to finance New Build ahead of any further borrowing. Therefore, the carrying balance from year to year remains low.
Debt Repayment Reserve	Sums set-aside to repay the initial “self-financing” debt; contributions to the Reserve start from 2018/19 in accordance with the debt repayment profile.

Key Variables and Assumptions

3.24 The Business Plan details the key variables on which the financial plan is based. These are summarised in the following table.

Cost inflation	Based on the latest economic forecast of 2.2% per year.
Annual rent increase	Inflation (as at September) as measured by the CPI +1% - based on the Government’s national rent guideline.
Void level	0.65% - based on historical levels.
Supported Housing Grant	£250,000 per year – cash limited.
Right to Buys	• 2014/15 - 20 • 2015/16 - 15 • 2016/17 - 15 • 2017/18 - 15 • 2018/19 - 13 • 2019/20 – 13
Capital Receipts	In accordance with current policy, all HRA retained receipts (after Pooling) are reinvested back into New Build as part of the “1-2-1” agreement with the Government.

New Build Units	• 2015/16 – 50 (financed) • 2016/18 – 60 (planned) • Up to 2024 – 130 (subject to resources)
Responsive and Cyclical Maintenance	£950 per property per year, plus £350,000 per year for disabled adaptations.
Capital Improvements	£27m investment programme over the first 5 years of the Plan and then £36,659 per property over 30 years as identified in the latest stock condition survey.
Interest Rates	Predominantly fixed; £10m variable debt at 0.7%, in 2014/15 rising to 1.1% in 2015/16 and to 2% in 2019 at maturity.
Minimum HRA Working Balance	£1m

Financial Risks

3.25 The Plan remains affordable if the above parameters and associated budgets are met. As planned at the outset of the self-financing framework, the HRA starts to generate surpluses after 2018/19 in order to repay debt.

3.26 The biggest risk is still considered to be future rent rises. The Financial Plan is fundamentally based on the Government's national rent guideline from 2015/16, i.e. inflation +1% year on year. If corresponding income levels are not achieved, this will have an effect on projected spending plans and investment.

New Build Programme

3.27 A Phase 1 programme has been approved and initial contractors appointed. Land has been identified and assembled and some initial works undertaken. The main projects are expected to commence in 2015/16.

3.28 This phase has a budget of £5.4m and is being financed mainly from resources already in the HRA and accumulated capital receipts. It is planned to provide up to 50 new properties.

3.29 The Plan also allows for the HRA to borrow a further £8m up to its debt cap over the life of the plan. This is designed to maximise the amount of New Build within available resources.

3.30 Although the Plan allows for a further 60 properties by 2018 and then 130 up to 2024, each phase in the future will need to be subject to a separate financial assessment and appropriate approval. The Business Plan Group recommended that alternative delivery models should be considered in the future to achieve the aims set out in the Plan.

Future Rent Levels

3.31 As previously reported, 2014/15 is the last year of rent restructuring and the convergence of all local rents to a level based on a national formula. From 2015/16, the Government's national rent setting policy is based on a guideline increase of inflation (as measured by the rate of CPI as at September) + 1%.

3.32 The Business Plan is based on this guideline. Therefore, all individual property rents, whether they have converged or not, will be increased from their actual level in 2014/15 based on this new guideline each year.

Proposed Rent Increase 2015/16

3.33 The Consumer Price Index (CPI) stood at 1.2% in September 2014. After adding on 1%, the proposed increase for 2015/16 is **2.2%.**

3.34 Based on this proposal, the average rent level would rise to £80.59 per week in 2015/16 (£79.23 in 2014/15). The average increase is £1.73, with the highest being £2.21 and the lowest £1.27 per week.

3.35 The highest rented property in the current housing stock would rise to £102.63 per week, with the lowest at £59.02 per week.

3.36 The Council does not have to adhere to the national guideline. However, if a lower increase is set, the impact on the Business Plan would need to be assessed as it could affect its longer term sustainability.

3.37 For every ½% reduction, this would reduce resources by approximately £60,000 per year and cumulatively over 10 years, this would equate to £600,000.

Limit Rents

3.38 If higher increase was set, then this would need to be considered against the *Limit Rent* set for the Council. This is effectively a cap (set by the DWP each year) that the Council's average rent needs to stay below, to avoid a financial penalty through loss of benefit subsidy for rent rebates.

3.39 For 2014/15, this limit was set at £79.58, which is just above the Council's average of £79.23. For 2015/16, the Limit Rent has been increased by the national guideline of 2.2%, to £81.33 per week.

3.40 The Council could increase its average rent by a further 74p per week (almost 1%) without being penalised. However, at that level, this would leave no leeway if the Council's average increased during the year through changes to overall stock numbers, for example right to buy sales. Changes can affect the average rent per week over a year.

Overall Rent Strategy

3.41 As part of the Business Plan, the following Rent Strategy was approved:

- Let all New Build and acquired properties at Affordable Rent Levels, i.e. 80% of Market Rent (*these rents do not count against the Limit Rent*).

- Let all existing properties at their “old formula rent” if still below this level where they become void and then subsequently relet (*this is a continuation of existing policy*).

- Increase the rent annually of all properties at the national guideline of CPI + 1%.

4.0 Financial Implications

4.1 As detailed in the report

5.0 Corporate Implications

5.1 There are no other legal, HR or other corporate implications apart from that considered in the report.

6.0 Community Implications

6.1 The proposed budgets and spending within the HRA provides the financial resources to enable many of the on-going services and Council priorities associated with council housing to be delivered to its tenants.

7.0 Background Papers

7.1 HRA Business Plan – December 2014:

http://south-derbys.cmis.uk.com/south-derbys/Meetings/tabid/70/ctl/ViewMeetingPublic/mid/397/Meeting/1730/Committee/367/Default.aspx