
REPORT TO:	OVERVIEW AND SCRUTINY COMMITTEE	AGENDA ITEM: 6
DATE OF MEETING:	10TH FEBRUARY 2010	CATEGORY: RECOMMENDED
REPORT FROM:	DIRECTOR OF CORPORATE SERVICES	OPEN
MEMBERS' CONTACT POINT:	KEVIN STACKHOUSE (595811)	DOC: u/ks/budget round 1011/policy reports/hra1011
SUBJECT:	HOUSING REVENUE ACCOUNT BUDGET, FINANCIAL PROJECTION and PROPOSED RENT INCREASE 2010/11	REF:
WARD(S) AFFECTED:	ALL	TERMS OF REFERENCE: HC 01

1.0 Recommendations

- 1.1 That an average rent increase of 2.05% for 2010/11 in accordance with Government guidelines be approved and is adjusted for individual tenants in accordance with the Rent Restructuring Formula, amended for the properties in 1.2 only.
- 1.2 That no change is made to current rents for those tenants (94) who although below their formula, would otherwise see a reduction in their current rent.
- 1.3 That the proposed estimates of income and expenditure for 2010/11 for the Housing Revenue Account are considered and referred to the Finance and Management Committee for approval.
- 1.4 That the updated financial projection, including the associated assumptions and analysis for the Housing Revenue Account to 2020 is considered and noted.

2.0 Introduction and 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 2010/11, together with an updated financial forecast to 2020. The report also sets out details of the proposed rent increase, together with the Government's subsidy settlement for 2010/11.
- 2.2 The report also includes an analysis of estimated income and expenditure with a comparison to the subsidy settlement for 2010/11.

The Principles of Housing Finance

- 2.3 Under the Local Government Housing Act of 1989, local authorities are required to account separately for the income and expenditure associated with council housing. Accounting regulations specify what can be charged to the Housing Revenue Account (HRA). This is designed to ensure that costs associated with the provision of council housing are financed separately to all other costs of the Council.
- 2.4 The Council is also required to maintain a 10-year business and financial plan to ensure that the service is sustainable in the longer-term. The HRA cannot operate in deficit and must maintain a minimum level of general reserves as a contingency. For South Derbyshire, this minimum level is currently an approved £1/2m.
- 2.5 The principal source of income in the Council's HRA is rent from tenants. At a national level, grant from central government also supplements income, i.e. Housing Subsidy. Rent levels are set nationally by the Government with rents at the Council currently being increased in phases (converged) year by year towards a national formula, known as "rent restructuring."
- 2.6 Housing subsidy is based on a system that is in principle "self-financing," designed to balance nationally, where authorities assessed as having good stock, low costs and/or high rent levels pay money over to a national pool. This is then redistributed to authorities who are assessed as having poorer stock, higher costs and/or lower rent levels.
- 2.7 Almost 2/3 of housing authorities, including South Derbyshire pay over to the national pool and are deemed to be in "negative subsidy." For this Council, the subsidy system assesses that income from rents is greater than expenditure on managing and maintaining the housing stock and takes this difference back to the national pool.
- 2.8 Within this, the system calculates a level of spending on management and maintenance, which for South Derbyshire is less than what is actually spent by the Council. As rents are fixed and limited to a national formula, this creates a deficit for the HRA.
- 2.9 It should be noted that it is widely accepted that the current subsidy system is outdated and affords too much volatility for local housing authorities to plan effectively in the longer-term. Consequently, the Government commissioned a review in 2008/09 and are currently consulting on proposals to change the current system. The main proposal would entail housing authorities "buying out" of the national system and become self-financing.
- 2.10 Councils are also set targets to maintain homes to a specified minimum decent standard. In recognition of this, the Government ring-fences resources in the subsidy system to provide a capital allowance to authorities to enable them to undertake rolling programmes of more significant improvements.

3.0 Executive Summary and Overall Commentary

The Financial Position Previously

- 3.1 Prior to 2009/10, the HRA had been operating in surplus in the short-term. However, the 10-year financial plan forecasted a longer-term budget deficit. To maintain anticipated levels of expenditure and based on assumed income, this deficit was to be financed by drawing on the relatively high level of general reserves on the HRA.
- 3.2 Clearly however, this is not sustainable. Previous plans have highlighted that by years 6 or 7, the HRA's reserves would fall below its minimum level of £1/2m and well in deficit before year 10. In addition, projections have effectively assumed a standstill budget from year to year.
- 3.3 The main reason for the deficit is that the Council budgets to spend more on management and maintenance compared to what it receives through the subsidy system. However, it should be noted that in independent evaluations, the Council's expenditure in the HRA has previously been low in comparison to other authorities.
- 3.4 This deficit is partly offset in other subsidy elements. Firstly, the amount received towards debt management is more than the HRA actually incurs. In addition, the level of empty (void) properties is generally less than that assumed in the subsidy calculation and this increases income, being a reflection of better performance locally.
- 3.5 In general, the HRA tends to spend within budget and in fact, in each of the last 3-years, day-to-day spending on repairs and maintenance has been well under that budgeted. This has enabled reserves to be maintained at a relatively high level compared to the minimum requirement of £1/2m.

Updated Position

- 3.6 Following the review of the HRA's base budget, the Government's subsidy settlement for 2010/11, together with their guidelines for rent levels next year, the 10-year financial projection has been updated.
- 3.7 This shows a worsening position. The HRA continues to operate in deficit with the first year under the £1/2m minimum reserve level being in 2015/16, compared to 2017/18 previously.
- 3.8 The main reasons for this is that firstly, the Council's average rent level will fall behind the Government's Guideline Rent from 2010/11. This is due to the fact that rent increases for many South Derbyshire tenants will be constrained within a maximum increase allowed under Government guidelines for 2010/11. Therefore, the HRA will not increase its overall income in line with that set in the subsidy settlement.

- 3.9 In addition, the Council's settlement for 2010/11 shows increases for management and maintenance allowances below the national average, but its guideline rent increase is above average.
- 3.10 A further factor is that the remaining contingency held in the housing capital receipts reserve of £300,000 to support the HRA, has now been earmarked for other capital expenditure. This would have sustained the HRA's reserve above the minimum level by a further year to 2016/17.

Rents

- 3.11 Changes have once again been made to rent restructuring with the convergence date now being brought forward from 2023/24 to 2012/13 due to the current low level of inflation. The proposed average rent increase for South Derbyshire tenants for 2010/11 is **2.05%**. However, many tenants will see increases above this, especially those who are still well below their formula rent. The largest increase is 2.82%.
- 3.12 The 2.17% is constrained to protect individual tenants. Without this, the unconstrained average increase would be **3.75%**. Effectively, this reduces the overall rental income in the HRA by approximately £156,000 per year (before any adjustments to subsidy) but 70% of the Council's tenants will benefit from the constraint.
- 3.13 In addition, this constraint will mean that many tenants will not converge with their rent formula in 3-years under the current system as their increase for 2010/11 is not in line with the step required. Depending on how the subsidy system takes this into account in future years, this will also reduce resources in the HRA to at least 2012/13, if the Council's actual rent remains behind the Guideline.

Subsidy

- 3.14 As expected, the Council's payment to the national pool will increase from £3,081,265 in 2009/10 to £3,305,079 (7.3%) in 2010/11. However, this is approximately £50,000 greater than estimated in the previous projection, mainly due to lower increases in management and maintenance allowances.
- 3.15 The subsidy system assesses that the Council's HRA is in surplus, with the associated payment to the national pool effectively being the largest expenditure item in the HRA.
- 3.16 Although it is widely recognised that the current subsidy system has shortcomings, it is still a significant factor for the Council's HRA. Therefore, it is important to analyse the key assumptions and changes to subsidy, including how this compares to the actual costs and rent income in the HRA.
- 3.17 A summary of the subsidy settlement to the estimated HRA in 2010/11 is provided in the following table.

<u>Excluding depreciation, MRA and provision for inflation in the HRA</u>	HRA £	Subsidy £	Difference £
Repairs and Maintenance	3,026,176	2,824,373	201,803
Management Costs	1,613,654	1,351,679	261,975
Capital Charges	91,935	278,367	(186,432)
Less Rent Income	(9,660,103)	(9,674,406)	14,303
Total Surplus	(3,013,429)	(3,305,079)	291,650

3.18 The table shows that overall the subsidy settlement assumes that the actual HRA is in surplus by an additional £291,650 and takes this back to the national pool.

Summary

3.19 The updated 10-year projection continues to show that eventually, the Council's HRA will become unsustainable. In the absence of any other changes, this will require a detailed review of all expenditure. In addition, similar to other local authority services, housing is subject to the Government's efficiency target (cashable savings) of 4% of net expenditure in 2010/11.

3.20 Previous reports to this Committee have highlighted a low cost base compared to other housing authorities, but with limited scope for additional investment. Infact, this current budget continues to assume a "standstill" position.

3.21 However, a review of the current HRA Business Plan will be undertaken during 2010/11. This will include a review of all costs, included those charged from internal support services.

3.22 Clearly, whether the Council will be able to afford and become self-financing under Government proposals will be the key to future projections. The Council's analysis of this and a response to the Government's consultation were reported and considered by the Committee in October 2009. An announcement is now expected from the Government by the end of February 2010.

4.0 Detail

4.1 The detailed figures are set out in 3 appendices, from which the figures in the various analyses are taken from.

- **Appendix 1** - a summary of each main income and expenditure head within the HRA for 2009/10 to 2019/20, together with the yearly surplus/deficit and balance on the HRA's general reserve.
- **Appendix 2** – an analysis of how housing subsidy has been calculated.
- **Appendix 3** – which provides examples to demonstrate the effect of the 2010/11 proposed rent increases on groups of tenants.

Formulating the 2010/11 Base Budget

- 4.2 The estimates are generally based on service levels in 2009/10 continuing, and include any full year effects of previous year's growth and capital expenditure. However, any non-recurring and one-off items have been removed. A provision for inflation has been provided for repairs, staffing/management cost, together with fees and charges.

Forward Projection

- 4.3 The base budget has then been projected forward based on a number of assumptions regarding inflation, repairs spending and rent increases, etc. These are detailed later in the report.

HOUSING SUBSIDY (Appendix 2)

- 4.4 The amount of subsidy due to or paid by housing authorities is determined through a notional (or assumed) HRA based on a number of factors and formulae, concerning the housing stock. In summary, subsidy due to councils is made up as follows:
- Management and Maintenance Allowance (M&M), **plus**
 - Contribution to capital/debt charges, **less**
 - Assumed rental income (based on a Guideline Rent)
- 4.5 The system also allocates funding through a Major Repairs Allowance (MRA). This is funding to meet major and on-going improvements to the housing stock. Although distributed through the subsidy system, it is a capital allowance and does not form part of the HRA's income and expenditure.
- 4.6 The indicators used to allocate funding are designed to assess the need to spend on repairs and management, taking into account the type and condition of the housing stock, together with the affordability of rent locally. However, this has to be done with an overall national amount allocated for subsidy by the Government.
- 4.7 The system is in principle "self-financing," designed to balance nationally, where authorities with good stock, low costs and/or high rent levels pay money over to the national pot. This is then redistributed to authorities with poorer stock, higher costs and and/or lower rent levels.
- 4.8 Almost 2/3 of housing authorities, including South Derbyshire pay over to the national pot and are deemed to be in "negative subsidy." For this Council, the subsidy system recognises that income from rents is greater than expenditure on managing and maintaining the stock and takes this difference back to the national pool.

The 2010/11 Subsidy Settlement

- 4.9 The main point arising from the national settlement for 2010/11 is that on average, it is neutral. This is because M&M allowances have been increased by an average of 3.05% (money due to councils), whilst guideline rents have been increased by an average of 3.1% (money paid by councils). The MRA has been increased by an average of 2.25%.
- 4.10 However, it has been estimated independently, that approximately £100m will be paid back in negative subsidy nationally in 2010/11, a similar figure to that in 2009/10. Inevitably, some Councils may find themselves worse off compared to their current position.

Major Repairs Allowance (MRA)

- 4.11 The Council's allowance per property has been increased from £611.36 in 2009/10 to £618.71 in 2010/11 (1.2%). This is below the average increase nationally of 2.25%.

- 4.12 In cash terms (after allowing for a reduction of 6 properties through Right to Buy) this equates to an increase of approximately £19,000. The total capital allowance for council housing in 2010/11 is £1,914,907.

Management and Maintenance (M&M) Allowances

- 4.13 The average increase nationally is 3.05% for both management and maintenance allowances. The Council's increases are shown in the following table.

	MANAGEMENT	MAINTENANCE
Allowance 2009/10	£428.12	£902.62
Allowance 2010/11	£436.73	£912.56
Percentage Increase	2.01%	1.10%

- 4.14 The increases are again below the national average. Based on the average number of council properties used for subsidy purposes, i.e. 3,095, this increases resources in 2010/11 by just under £50,000 compared to 2009/10.

Guideline Rents

- 4.15 Guideline rents will increase on average, nationally by 3.1% in 2010/11. The effect on the Council is shown in the following table – i.e. the Council's guideline rent as set by the subsidy system.

2009/10	£59.39 per week
2010/11	£61.34 per week
Increase	£1.95 per week (3.3%)

4.16 The Council's guideline has been increased slightly above the national average at 3.3%. Based on the number of council properties and a 2% allowance for voids, this reduces resources in the notional account in 2010/11 by approximately £290,000 compared to 2009/10.

Overall Position

4.17 After allowing for changes in the other components, overall, the Council's base contribution to the national pool will increase by approximately £224,000 in 2009/109 to just over £3.3m (net of the Major Repairs Allowance).

RENT RESTRUCTURING AND PROPOSED RENT INCREASE 2010/11

4.18 Rent restructuring was introduced in 2001/02, with the aim of basing rents on property values, local wages and the number of bedrooms in a property. In addition, it is also intended to eliminate differences between rents set by local councils and those set by other housing providers in each area.

4.19 Rents for individual properties are calculated in accordance with a formula (called the Formula Rent) based on the above factors.

4.20 In recognition that the new system could substantially change individual rents over-night, the Government's policy was to phase in changes between actual rents being paid at that time and those calculated under the national formula. Full convergence was originally planned by 2011/12 (i.e. over a 10-year period).

4.21 Changes since then have updated the formula, in particular to reflect increasing property values. Caps on maximum increases have been implemented in some years and the convergence period has been moved to 2016/17 and then to 2023/24 last year.

4.22 This latest change was to recognise that rent restructuring has increased average rents in the local authority sector as they are brought into parity with other housing providers. It was also made in the context of a higher level of inflation a year ago. The principle is that high levels of inflation push convergence away, low or negative levels, brings the convergence date forward.

4.23 Extending convergence is designed to spread the effects of future increases to avoid hefty rent rises for individual tenants. This is the case for South Derbyshire as on average, actual rents are well below formula rents.

Changes for 2010/11

4.24 The Formula Rent is changed each year based on the rate of inflation as measured by the Retail Price Index (RPI) in the September proceeding the next financial year. In line with Government policy, a further ½% is added to reflect a real terms increase.

4.25 RPI stood at a negative (-) 1.4% as at September 2009. After adding back the ½%, formula rents have been decreased overall by 0.9%. Consequently, this has the effect of once again bringing forward the date of convergence to 2012/13, i.e. 3 years.

4.26 Consequently, the Council's average formula rent decreases from £68.28 to **£67.68** per week in 2010/11.

4.27 To adhere to the new rent convergence date, after applying the reduction of 0.9%, individual tenants will be moved 1/3 of the way between their actual and updated formula rent subject to a maximum increase, set by the Government, calculated as follows:

- RPI + ½% + £2 per week

Actual Rent Increase

4.28 The average actual increase for tenants in South Derbyshire for 2010/11 is therefore proposed at £1.23 per week or **2.05%**. The average rent will rise from £59.99 to **£61.22** per week in 2010/11. This is below the Formula of £67.68, a difference of 9.5%, although this difference has reduced from nearly 14% in 2009/10.

4.29 However, within this average increase, there is a range of changes and these are summarised in the following table.

CHANGE (IN POUNDS)		CHANGE (IN % TERMS)	
Fall of more than 50p per week	6	Fall of more than 1%	6
Fall of up to 50p per week	0	Fall of up to 1%	0
No rise or fall	108	No rise or fall	108
Rise of up to 50p per week	203	Rise of up to 1%	245
Rise between 51p and £1	335	Rise between 1% and 2%	383
Rise between £1.01 to £1.50	2,403	Rise between 2% and 2.5%	1,821
Rise of more than £1.50	5	Rise of more than 2.5%	497
Total Properties	3,060		3,060

Largest fall – 77p per week – 1.5%

Maximum rise - £1.52 per week – 2.8%

Specific Effects for South Derbyshire Tenants

- 4.30 The above table shows that a handful of tenants (6) will see a fall in rent as their actual level is above their formula. An example of how this works is shown in **Appendix 3 (example 1)**.
- 4.31 It is proposed that for 94 tenants, the Council diverts from the rent restructure policy for 2010/11 and does not change their current rent. This proposal is to avert an anomaly whereby these tenants, although below their formula, would see a reduction in their current rent.
- 4.32 This is due to the fact that the stepped increase of 1/3 between the updated actual and formula rents does not make up for the (minus) 0.9% reduction in their current rent.
- 4.33 An example of how this works is also shown in **Appendix 3 (example 2)**. These tenants are in fact not far from the formula and the overall difference in rent income to the HRA is fairly small, i.e. it gains by £700 for 2010/11.
- 4.34 This also avoids greater increases for these tenants in future years to catch up their formula rent.

The Effect of the Rent Constraint

- 4.35 However, a bigger issue is the amount of tenants subject to a maximum increase or rent constraint due to a significant difference between their current rent and their formula. The reduction in rent levels by 0.9% overall, although clearly offering protection to individual tenants, reduces the amount of rent income for the HRA. An example of how this works is also provided in **Appendix 3 (example 3)**.
- 4.36 In total, 2,169 tenants (70%) are affected by the constraint. On average, this equates to “lost” rent to the HRA of approximately £3,000 per week, or £156,000 in the year for the HRA (before any adjustment in subsidy).
- 4.37 The consequences for a large proportion of the Council’s tenants is that they will not converge in 3-years as their current rent will not be moved by the full 1/3 in 2010/11. They will now lag further behind their formula and tenants may now take 4, 5, or even 6 years under the current system.

Comparison to the Guideline Rent

- 4.38 As highlighted, the proposed rents provide an average of £61.21, compared to the Guideline of £61.34. Although this is only 13p per week, it still reduces overall rent in total by approximately £20,000 per year.
- 4.39 The effect in future years depends on how the subsidy system takes this into account. Potentially, this could reduce resources further in the HRA to at least 2012/13, as the Guideline will continue to move further away from actual rents if actual rents are constrained. [Page 10 of 18](#)

4.40 By 2012/13, the difference will be 66p per week, which equates in total to approximately £105,000 per year for the HRA.

Flexibility

4.41 Although the Council does not have to follow the Government guideline for rents, the HRA would be penalised through the subsidy system by not following the Government's policy. For example, where rents are set higher, the subsidy mechanism would withdraw grant for Rent Rebates and this would become an additional cost on the HRA.

4.42 The Council could potentially increase the rent so that the average comes up to the Guideline. However, this is not practical as many tenants are already constrained and breaking the constraint would most likely, be open to challenge.

4.43 A proposal above effectively diverts some tenants from the guidelines, although this is not significant given the small number and rent total involved. Consequently, this does not affect the average rent level and avoids greater increases for these tenants in future years to catch up their formula rent.

4.44 Setting lower rents would not in itself reduce subsidy. However, it would reduce income in the HRA and put average rents further behind the formula.

Proposed Changes to the Policy

4.45 Proposals are currently being considered to change the Council's rent setting policy. This would entail diverging from the national policy by moving new tenants direct to the formula rent on a re-let.

4.46 This would increase overall rent to the HRA. A full analysis of this option will be subject to a separate report at the next meeting of the Committee.

HRA FINANCIAL FORECAST TO 2020 – OVERVIEW (APPENDIX 1)

4.47 The Council is directed by the Government's Regional Office to plan and monitor its longer-term financial position over 10 years on the HRA (on a rolling basis) and to maintain at least its minimum reserve balance. The Council's financial strategy sets this minimum contingency reserve at £1/2m.

4.48 The updated projection continues to show a worsening position. The HRA continues to operate in deficit with the first year under the £1/2m minimum level being in 2015/16, compared to 2017/18 previously.

4.49 The main reasons for this are the consequences of the subsidy settlement compared to the projected spending, together with the proposed rent increase for 2010/11 as detailed earlier in the report. In addition, resources previously allocated as a contingency for HRA purposes of £300,000 have been earmarked as a contingency for other capital purposes.

Summary of Main Assumptions, Sensitivity and Risks

4.50 Clearly a forecast of this length does need to be treated with a certain degree of caution, and assumptions need to be made that could in the future change.

4.51 The Council uses a financial model that has been developed with an external agency. This automatically updates income and expenditure based upon assumptions regarding the different variables. Assumptions for inflation and interest rates have been updated to take account of the Government's Pre-Budget (December 2009) Report.

4.52 The current assumptions, including those estimated for the 2010/11 base budget are set out below for the major categories of income and expenditure in the HRA. This also includes an analysis of income and expenditure compared to the subsidy settlement for 2010/11.

Housing Repairs

4.53 Provision for inflation is made above general levels to reflect the traditionally higher than average inflation increases in the building sector. Allowances included in the projection for inflation on the base budget are as follows:

- 2010/11 – 3.25%
- 2011/12 – 2.5%
- 2012/13 – 3.5%
- 2013/14 onwards – 3.75%

4.54 These indices are 1% above the Government's general measure of inflation, i.e. the Gross Domestic Product (GDP) Deflator used in the Pre-Budget Report.

4.55 Over the last 3 years, actual expenditure on repairs compared to budget and that received in subsidy, is summarised in the following table.

Year	HRA Budget £	HRA Actual £	HRA Variance £	Subsidy £	Allowance per Dwelling £:p	Number of Dwellings
2006/07	2,900,800	2,643,546	- 257,254	2,599,136	802.45	3,239
2007/08	3,014,860	2,897,584	- 117,276	2,678,194	843.26	3,176
2008/09	3,150,530	3,090,190	- 60,340	2,706,471	865.24	3,128
2009/10	3,127,000	3,127,300	0	2,799,025	902.62	3,101

Note – for 2009/10 – actual is based on latest estimates and assumes spending is on budget; the budget includes a provision for inflation of 4.5%

4.56 There are several points raised by these figures. Firstly, spending has been lower over the last 3-years. As previously reported, in a demand led budget, significantly fewer repairs have been undertaken. This may be a reflection of the investment the Council has put into planned maintenance over recent years, with a pattern of fewer responsive repairs emerging.

- 4.57 In addition, milder weather conditions in recent winters, together with a reduction in emergency repairs and property numbers have also helped.
- 4.58 The increase in actual spending between 2006/07 and 2009/10 (estimated) is 7.8%. The amount reimbursed in subsidy has almost increased by this amount over the same period, i.e. by 7.7%.
- 4.59 The increase in allowance per property has actually increased by 12.5% (£802 to £902) although this has not fed into cash received as property numbers have fallen.
- 4.60 The increase in the subsidy allowance highlighted previously of 1.1% for 2010/11 is the lowest for many years. This provides resources for repairs of £2,824,373 compared to the HRA's proposed spending budget of £3,244,000 (including inflation of 3.75%). The difference of approximately £420,000 is greater than that in 2006/07 of approximately £300,000.

Stock Condition and the Decent Homes Standard

- 4.61 However against this, it should be noted that the latest (2009) Stock Condition Survey for Council Houses identifies a potential £12m shortfall in capital resources to maintain the stock in the longer-term. It is considered that this will place pressure on meeting the Decent Homes Standard beyond 2012/13.
- 4.62 This capital spend has previously been supported direct from the HRA Planned Maintenance Budget and this is reason why the current level of repairs budget overall is maintained.

Management and Sheltered Accommodation Costs

- 4.63 These are largely staffing costs, with the following provisions for inflation on the base budget.
- 2010/11 – 1.25%
 - 2011/12 – 1.25%
 - 2012/13 – 2.00%
 - 2013/14 onwards – 3.00%
- 4.64 The lower provisions over the next 2-years reflect the Government's intention to minimise pay increases in the public sector as set out in the Pre-Budget Report.
- 4.65 The total base budget for 2010/11, net of income for Lifelines and Supporting People Contributions is £1,613,654. This also includes recharges for support services. The amount provided for subsidy in 2010/11 is £1,351,679, a difference (shortfall) of approximately £262,000.

Housing Rents

4.66 The following assumptions have been made to increases in the Council's actual and guideline rents:

- 2011/12 – 2.00%
- 2012/13 – 3.00%
- 2013/14 onwards – 3.25%

4.67 This includes a real-terms increase of ½% per year in accordance with current Government Policy. Critically, the projection assumes that rent convergence will be achieved in 3-years, by 2013/14. To achieve this, average increases, in total, will need to be as follows:

- 2011/12 – 5.26%
- 2012/13 – 6.10%
- 2013/14 - 6.17%
- 2014/15 - 4.17%
- 2015/16 onwards – 3.25% (as above – after convergence)

4.68 Effectively, a further 3% increase per year over and above inflation will be required in order to converge in 3-years. However, as previously highlighted, 70% of tenants may not converge as their current rent will not be moved by the full 1/3 in 2010/11. They will now lag further behind their formula and tenants may now take 4, 5, or even 6 years under the current system.

4.69 As previously shown, for the HRA overall, this reduces potential resources. If convergence does not occur in accordance with the current timeframe, then further resources would be lost.

4.70 However, this will depend on the subsidy settlement each year and the rate of inflation used by the Government as the basis to increase rents. To a certain extent, this is not critical to the HRA – the key factor is that the Guideline does not move further away from the actual as the subsidy system assumes that the Council generates this rent level (at Guideline).

Comparison of Actual Rent Income to that Assumed in Subsidy

4.71 Based on an average rent increase of 2.05% and after allowing for a void rate of 0.85%, the HRA will generate £9,660,103 in rental income for 2010/11. This compares to assumed rent income for subsidy purposes of £9,674,406, only £14,403 higher.

4.72 However, within this, there are some significant variances which offset each other, as follows:

- Higher property numbers in the subsidy settlement + £110,000
- Guideline rent above the Council's actual rent + £20,000
- Offset by better performance of properties - £116,000

- 4.73 Firstly, the subsidy system does not use the most up-to-date property numbers as they are based on those in the previous year and for 2010/11, the number as at 1st April 2009 (i.e. the Council's opening stock for that year).
- 4.74 During 2009/10, the Council's average stock will reduce by 34, mainly due to the decommissioning of 30 units associated with the Extra Care Development in Swadlincote. The subsidy system assumes an average stock of 3,095 dwellings (which is fixed) when in practice the Council will generate rent from 3,061 in 2010/11.
- 4.75 Based on a guideline rent of £61.34, the subsidy system assumes that the Council will collect approximately £110,000 more in rent than it actually will.
- 4.76 It should be noted that in calculating the allowances for M&M, the higher property number is also used and this benefits the HRA. However, the amount involved is much less at approximately £45,000 in 2010/11.
- 4.77 The subsidy system also assumes an additional £20,000 due to the difference in the Council's actual rent compared to the Guideline of 13p in 2010/11, as analysed earlier in the report.
- 4.78 However, the Council's performance on void properties is significantly better than that assumed for Subsidy. The Council's void rate is estimated at 0.85% for 2010/11, compared to a 2% allowance in the subsidy settlement. This equates to "additional" rent of approximately £116,000.

Capital Charges

- 4.79 Having paid off its Government debt in 2004/05, the Council only has outstanding credit in the form of Covenant finance which applies to the HRA. This arrangement entered into many years ago (circa 1980s) provided resources to deliver substantial improvements at that time to the housing stock, mainly central heating installations and kitchen replacements.
- 4.80 The subsidy system recognises this arrangement and reimburses the cost of servicing the credit that is charged to the HRA. The final payments are due in 2011/12.
- 4.81 Although the HRA is effectively debt free, the system does not recognise that the debt may have been repaid or rescheduled. Consequently, the HRA is charged (by the Council's General Fund) with debt charges, but for which the cost is recognised by the subsidy system.
- 4.82 Suffice to say that this can cause confusion, especially as the base used to calculate the charges is notional. The system recognises that under previous borrowing approvals, the Council has taken on debt for which the Government supports through the subsidy system on an on-going basis.
- 4.83 Historically however, actual debt outstanding changed from the assumed level as loans were taken out at different times and were rescheduled or repaid.

- 4.84 This has created a benefit in the current system for the HRA as the interest charged is based on debt outstanding of £2m, whilst the subsidy system reimburses interest based on debt outstanding of £9m. Even at current low interest rate levels, this will provide resources to the HRA of approximately £186,000 in 2010/11.
- 4.85 This is a key factor for the HRA, as at higher rates of interest, this difference increases and helps to offset the “negative” balances on M&M allowances in particular.
- 4.86 The interest rate used is known as the Consolidated Rate of Interest (CRI) and is based on a LIBID rate of interest as notified by the Government. The following rates have been used in the 10-year projection.
- 2009/10 – 2.00%
 - 2010/11 – 2.50%
 - 2011/12 – 3.50%
 - 2012/13 – 4.50%
 - 2013/14 – 5.50%
 - 2014/15 onwards – 6.50%

Overall Comparison of Income and Expenditure Compared to Subsidy

- 4.87 The subsidy system assumes that the Council’s HRA is in surplus, with the associated payment to the national pool effectively being the largest expenditure item in the HRA. Although it is widely recognised that the current subsidy system has short-comings, it is still a significant factor for the Council’s HRA.
- 4.88 Therefore, it is important to analyse the key assumptions and changes to subsidy, including how this compares to the actual costs and rent income in the HRA.
- 4.89 A summary of the subsidy settlement to the estimated HRA in 2010/11 is provided in the following table.

<u>Excluding depreciation, MRA and provision for inflation in the HRA</u>	HRA £	Subsidy £	Difference £
Repairs and Maintenance	3,026,176	2,824,373	201,803
Management Costs	1,613,654	1,351,679	261,975
Capital Charges	91,935	278,367	(186,432)
Less Rent Income	(9,660,103)	(9,674,406)	14,303
Total Surplus	(3,013,429)	(3,305,079)	291,650

- 4.90 The table shows that overall the subsidy settlement assumes that the actual HRA is in surplus by an additional £291,650 and takes this back to the national pool.

Proposed Changes to the National System

- 4.91 It should be noted that it is widely accepted that the current subsidy system is outdated and affords too much volatility for local housing authorities to plan effectively in the longer-term. Consequently, the Government commissioned a review in 2008/09 and are currently consulting on proposals to change the current system.
- 4.92 In summary, this would entail housing authorities buying out of the national subsidy system to become self-financing. The “buy-out” would entail each authority taking on and paying for a share of the national housing debt. For the Council, this would mean no payment to the national pool, but this would be replaced with a debt repayment.
- 4.93 Clearly, whether the Council will be able to afford and become self-financing under Government proposals will be the key to future projections. The Council’s analysis of this and a response to the Government’s consultation were reported and considered by the Committee in October 2009. An announcement is now expected from the Government by the end of February 2010.

Overall Summary

- 4.94 Clearly, all of this together continues to provide challenges for managing the HRA.
- 4.95 Although the short-term position continues to remain fairly sound, the longer-term viability of the HRA is still very much questionable. This is compounded by the uncertainties within the current funding system.
- 4.96 Previous reports to this Committee have highlighted a low cost base compared to other housing authorities, but with limited scope for additional investment. Infact, this current budget assumes a “standstill” position.
- 4.97 Finally, the self-financing proposals will be a key factor, but this will depend on the affordability of the “buy-out” compared to the degree of, and when, future benefits accrue for South Derbyshire.

5.0 Financial Implications

5.1 As detailed in the report

6.0 Corporate Implications

6.1 There are no other direct legal, personnel or property implications apart from that considered in the report.

7.0 Community Implications

7.1 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 the local community.

8.0 Background Papers

8.1 Department for Communities and Local Government - Housing Subsidy Determination (and associated papers) 2010/11, available at:
<http://www.communities.gov.uk/housing/publications/consultations>

8.2 The Government's Pre-Budget Report (December 2009), available at:
http://www.hm-treasury.gov.uk/prebud_pbr09_repindex.htm

8.3 The Government's proposals for Self-Financing and the Council's response, available at:
<http://cmis.south-derbys.gov.uk/CmisWebPublic/Binary.ashx?Document=5478>