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<b>REPORT TO:</b>	<b>HOUSING AND COMMUNITY SERVICES COMMITTEE (SPECIAL - BUDGET)</b>	<b>AGENDA ITEM:</b> 7
<b>DATE OF MEETING:</b>	12th JANUARY 2006	<b>CATEGORY:</b> <b>RECOMMENDED</b>
<b>REPORT FROM:</b>	<b>DIRECTOR OF CORPORATE SERVICES</b>	<b>OPEN</b>
<b>MEMBERS' CONTACT POINT:</b>	<b>KEVIN STACKHOUSE (595811)</b>	<b>DOC:</b> u/ks/budget round 0607/hra budget report 06
<b>SUBJECT:</b>	<b>HOUSING REVENUE ACCOUNT BUDGETS, FINANCIAL PROJECTIONS &amp; PROPOSED RENT INCREASE 2006/07</b>	<b>REF:</b>
<b>WARD(S) AFFECTED:</b>	<b>ALL</b>	<b>TERMS OF REFERENCE:</b> HC01

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## **1.0 Recommendations**

- 1.1 That an average rent increase of 5% for 2006/07 in accordance with Government guidelines be approved and is adjusted for individual tenants in accordance with the Rent Restructuring Formula.
- 1.2 That the proposed estimates of income and expenditure for 2005/06 and 2006/07 for the Housing Revenue Account are considered and referred to the Finance and Management Committee for approval.
- 1.3 That the updated financial forecast for the Housing Revenue Account to 2015 is noted.

## **2.0 Purpose of Report**

- 2.1 To detail the Housing Revenue Account's (HRA) probable out-turn for 2005/06, the base budget for 2006/07 and an updated financial forecast to 2015. It also sets out details of the proposed rent increase for 2006/07.
- 2.2 In addition, the report provides details of the Government's subsidy settlement for 2006/07 and 2007/08 and fairly significant changes to rent restructuring.
- 2.3 Housing finance and the regulations that govern it can be complex. An overview of the framework is set out in **Appendix 3** as background to the report.

## **3.0 Executive Summary**

- 3.1 The overall forecast for the HRA continues to show a stronger financial position especially in the shorter term. This helps the account to become more sustainable by 2015 (the Government's indicative target date). The balance on the HRA's reserve is

forecasted to fall from its current level of £1.35m to just above £1/2m by 2015, which is the minimum level required to demonstrate the sustainability of the HRA longer term.

- 3.2 However, this is still reliant on the use of £1m of capital resources to finance planned maintenance spending over the next 3-years. Clearly, without this, the overall account would fall into deficit by 2015.
- 3.3 In addition, the forecasted deficit on the HRA increases from 2008/09 and is forecasted to be around £370,000 per year by 2015, i.e. overall core expenditure will still be above overall income.
- 3.4 The previous reported forecast in July 2005, showed a negative balance of approximately £400,000 by 2015 (including the £1m capital support). The approved Business Plan for the HRA produced in November 2005, indicated a more favorable position. This seems to have been borne out following the Government's financial settlement and changes to rent restructuring, albeit in a different way.

### **Increased Rental Income**

- 3.5 The main reason for the more favorable position is an increase in rental income for the HRA. The Government has rebased rent restructuring and this will result in larger than usual rent increases in 2006/07, especially those for bigger properties (3 or more bedrooms).
- 3.6 The average rent increase for the Council in 2006/07 (if approved) will be 5%, with an average of 3% per year (as currently set out by the Government) up to 2012. Not all council tenants will see this level of increase, some will be lower and some higher, depending on how their current rent compares to the target rent.

### **Increased Payments to the National Pool**

- 3.7 On the negative side, the overall subsidy settlement for 2006/07 (and beyond) will require increases in payments to the National Housing Pool. The Council has been awarded fairly high increases in its management and maintenance allowances of 11 and 12% respectively for 2006/07. However, this has been more than offset by a claw back (through the subsidy system) of rent income.

### **Housing Repairs**

- 3.8 In addition, the current base estimate for expenditure on housing repairs has been increased by approximately £150,000. This reflects expenditure in the last 2 years where actual spending levels have exceeded that estimated.

## **4.0 Detail**

- 4.1 The detailed figures are set out in 2 appendices, as follows:

- **Appendix 1** - a summary of each main income and expenditure head within the HRA for 2005/06 to 2014/15, together with the yearly surplus/deficit and balance on the HRA's reserve.
- **Appendix 2** – an analysis of how housing subsidy has been calculated.

## 2005/06 Probable Out-turn

- 4.2 The updated estimate following the 2004/05 final accounts that was reported in July 2005, showed an overall surplus (after capitalising planned maintenance works) of approximately £319,000. The probable out-turn now shows an overall surplus of around £387,000. The main reasons for the increase on the estimated surplus are set out in the following table.

Increased rent due to reduction in empty properties and house sales	£90,000
Lower overall management costs (estimated at approximately £1.5m)	£55,000
Review and reduction in council tax liability on empty properties	£30,000
Increase in other income and interest	£25,000
Other reductions - mainly capital costs transferred from the Gen. Fund	£20,000
<b>Sub Total</b>	<b>£220,000</b>
Less - Increase in overall repairs budget to reflect actual spending	£150,000
<b>Overall increase in estimated surplus</b>	<b>£70,000</b>

## Basis of 2006/07 Estimates

- 4.3 The budget for 2006/07 has initially been compiled at November 2005 (today's) prices. An allowance for inflation has then been added where this is considered unavoidable, to cover for price increases to March 2007. This calculates the cash limit estimate for 2006/07, in which budgets should be managed.
- 4.4 Inflation measures are based on data available from HM Treasury for various categories of income and expenditure. The assumptions built into estimates are as follows:
- Employee Costs – 2.95% (as per the existing national pay settlement)
  - Responsive Repairs and Maintenance – 2.5%
  - Planned Maintenance – 5%
  - Utilities – 5%
  - Business Rates – 2.7%
  - Fuel – 5.6%
  - Insurance Premiums – 2.7%
  - Other Supplies and Services – 2.7%
  - Office Expenses (equipment, stationery, etc.) – cash limited
  - Other Categories – 2.68% (the Government's general measure of inflation)
  - Other income (excluding rents) - 2.68%
- 4.5 The estimates are also based on service levels in 2005/06 continuing, and include any full year effects of previous year's growth and capital expenditure. However, any non-recurring items have been removed.

## HOUSING SUBSIDY (Appendix 2)

4.6 The main points arising from the Government's national housing subsidy settlement for 2006/07 and 2007/08 are summarised below:

- Extensive volatility resulting from the re-shaping of management and maintenance (M&M) allowances and the implementation of a rent restructuring review.
- Resulting in bigger than usual rent increases (especially for larger properties).
- A further tightening of the national resources available for the management of council housing.
- Sharp regional differences.
- But increases in capital funding through the Major Repairs Allowance.

### Major Repairs Allowance

4.7 The Council's allowance per property has been increased from £532 in 2005/06 to £558 in 2006/07 (4.9%). In cash terms (after allowing for a reduction in properties) this equates to approximately £50,000.

### Management and Maintenance Allowances

4.8 Allowances have been increased nationally by 9%, although there are sharp regional differences. The East Midlands region is generally set to gain. The Council fairs very well as shown in the following table.

	Management	Maintenance
Allowance 2005/06	£339.80	£716.03
Actual Allowance 2006/07	£378.31	£802.45
Percentage Increase	11.33%	12.1%

4.9 Based on the number of council properties, this increases resources in 2006/07 by approximately £327,000 compared to 2005/06.

### Guideline Rents

4.10 Through this mechanism, the Government control rent restructuring and it is the amount of money the system assumes an authority collects in rent. This amount is deducted from M&M allowances and if it is greater (which it is for the Council) then it is deemed "negative subsidy" and the net amount is paid to the national pool.

4.11 Due to a review of the national rent restructuring policy, guideline rents will increase by 9.5% in 2006/07. This is more than the increases in M&M allowances nationally, of 9%.

4.12 The effect on the Council is shown in the following table – i.e. the Council's guideline rent as set by the subsidy system.

2005/06	£47.01 per week
2006/07	£51.83 per week
Increase	10.25%

4.13 Based on the number of council properties, this reduces resources in 2006/07 by approximately £625,000 compared to 2005/06. Overall, the Council's base contribution to the national pool will increase by approximately £320,000 in 2006/07.

### **RENT RESTRUCTURING AND PROPOSED RENT INCREASE 2006/07**

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

4.15 In recognition that this could substantially change individual rents over-night, the Government's policy is to phase in changes between actual rents being paid today and those calculated under the national formula. Full convergence is planned by 2012 (i.e. over a 10-year period).

4.16 In 2004, the Government undertook a review of their policy, in particular to change parts of the formula in order to update it for:

- Larger properties (to increase the weighting for properties with 3 or more bedrooms).
- To reflect increases in property values since 2000.

4.17 The proposals were not implemented for 2005/06, but will now be introduced from 2006/07. All authorities will need to recalculate formula rents for each tenant back to 2001/02 and update it to 2006/07 in accordance with the changes highlighted above.

4.18 In addition, the Government have set a national average increase in rents of 3.2% (2.7% inflation + 0.5% real terms increase).

4.19 After recalculating formula rents and applying the 3.2% increase, individual tenants will see their rent change depending on how their current rent compares to their new target calculated under the updated formula.

4.20 Most tenants will see an increase in rent. However, some tenants will see lower increases due to their current rent being closer to their target.

### **Caps on Increases**

4.21 In addition, caps have been placed on individual increases for tenants and on the overall increase for each authority. These caps are:

- Individual tenants - 2.7% + ½% + £2 per week

- The Council's overall average rent cannot increase by more than 5%.

4.22 Some tenants will be "protected" by the above cap. However, at an overall level, the Council will be constrained by the "5% cap." Under the revised formula, the Council's average rent would increase from £49.79 per week in 2005/06, to £52.82 per week in 2006/07 – an increase of 6%. This will be capped at 5% to an average of £52.27 per week.

4.23 Therefore, the average increase for the Council is 5%, which is approximately £2.50 per week. However, within this, there is a range of changes and these are summarised in the following table.

<b>Level of Increase</b>	<b>Number of properties affected</b>
Less than £1 per week (up to 2%)	311
Between £1 to £2 per week (up to 4%)	587
Between £2 and £3 per week (up to 6%)	966
Over £3 per week (highest is £3.84 per week – 7.1%)	1,334
<b>Total Properties</b>	<b>3,198</b>

4.24 In line with the rent restructuring formula and its effect on the Council, the lower increases relate to smaller and properties in sheltered accommodation. The higher increases relate to larger (3 and 4 bedroom) properties.

### **Additional Resources**

4.25 The net effect on the Council is that the average increase of 5% should generate additional rental income of approximately £330,000 in 2006/07 compared to current levels. The Government are currently reviewing whether they will compensate authorities who are constrained by the 5% limit. The amount "lost" to the HRA due to this constraint is approximately £57,000 per year.

### **Flexibility?**

4.26 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. This would become an additional cost on the HRA.

4.27 Setting lower rents would not in itself reduce subsidy. However, the mechanism assumes that rent restructuring is being applied and builds this into assumed rent levels. Setting a lower level will therefore reduce overall rent to the HRA. For example, constraining the average increase to 3%, would "cost" the HRA approximately £177,000 per year. In addition, the Council would not achieve rent harmonisation by 2012.

## HRA FINANCIAL FORECAST TO 2015 – OVERVIEW (APPENDIX 1)

- 4.28 The net effect of the changes to subsidy and rent restructuring, are overall, more favourable to the HRA. This helps to strengthen its financial position especially in the shorter term and this helps the account to become more sustainable by 2015 (the Government's indicative target date).
- 4.29 The balance on the HRA's reserve is forecasted to fall from its current level of £1.35m to just above £1/2m by 2015, which is the minimum level required to demonstrate the sustainability of the HRA longer term.
- 4.30 However, this is still reliant on the use of £1m of capital resources to finance planned maintenance spending over the next 3-years. Clearly, without this, the overall account would fall into deficit by 2015.
- 4.31 In addition, the forecasted deficit on the HRA increases from 2008/09 and is forecasted to be over £1/2m per year by 2015, i.e. overall core expenditure will still be above overall income.
- 4.32 The previous reported forecast in July 2005, showed a negative balance of approximately £400,000 by 2015 (including the £1m capital support). The approved Business Plan for the HRA produced in November 2005, indicated a more favorable position. This seems to have been borne out following the Government's financial settlement and changes to rent restructuring, albeit in a different way.
- 4.33 Clearly, a forecast of this length does need to be treated with a certain degree of caution, and assumptions need to be made that will in the future most likely change. Factors such as housing subsidy and council house sales are outside the Council's control.

### Summary of Main Assumptions and Risks

- 4.34 The current assumptions beyond the current base budget from 2007/08 are set out below for the major categories of income and expenditure in the HRA.
- **Housing Repairs** – an increase of 5% in overall spending, to reflect the traditionally higher than average inflation increases in the building/maintenance sector. **In addition, the current expenditure level on repairs has been assumed to continue over this forecasting period.**
  - **General Management** – largely staffing costs, increased by 3% per year, assuming current service provision.
  - **Net Cost of Rent Rebates** – being phased out in accordance with rent restructuring by 2012.
  - **Rents** – target and actual rents increased by 3% per year. This is in accordance with Government plans.
  - **Council House Sales** – currently 60 per year, being reduced over the forecasting period to 24 per year by 2015. Clearly, this can be volatile and is subject to external factors outside the Council's control.

- **Management and Maintenance Allowances** – continuing real-terms increases of 1% per year in accordance with Government plans.
- **Supporting People Grant** – will be subject to on-going review by the administering body. The level of support could be reduced in accordance with national aspirations for efficiencies in this area. The longer-term projection assumes a freezing of the current base (income) budget.
- **Payment to the Government Pool** – arguably this is the biggest risk area especially as it is effectively outside the Council's control. The settlement for 2006/07 demonstrates the volatility of the system. The Council continues to fair well from increases in management and maintenance allowances, but it is the interplay between rents set nationally and those set locally, that has the greatest effect on the HRA.
- **National Resources** – following on from the above, the future level of resources for housing nationally beyond 2007/08 will be determined in the Government's Comprehensive Spending Review in 2006. Any potential effects on the Council will be closely monitored.

## 5.0 **Financial Implications**

5.1 As detailed in the report

## 6.0 **Corporate Implications**

6.1 None Directly

## 7.0 **Community Implications**

7.1 None Directly

## 8.0 **Background Papers**

8.1 ODPM - Housing Subsidy Determination (and associated papers) 2006/07 and 2007/08.