

CABINET

Future Housing Regeneration Funding Options and Medium Term Council Housing Rent Policy

04 September 2012

Report of Head of Resources and Head of Health and Housing Services

PURPOSE OF REPORT

To consider options for adopting a medium term council housing rent policy and wider medium term financial strategy for council housing, in context of housing regeneration priorities and potential future funding options. Members have reaffirmed that the strategic housing regeneration priorities for the foreseeable future are:

- (a) To increase the supply and delivery of affordable housing schemes.
- (b) To complete existing unfinished schemes in the West End (the completion of outstanding housing regeneration projects at Chatsworth Gardens and Marlborough Road/Bold Street).
- (c) To bring empty properties back into use.

Key Decision	<input checked="" type="checkbox"/>	Non-Key Decision	<input type="checkbox"/>	Referral from Cabinet Member	<input type="checkbox"/>
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Date Included in Forward Plan	July 2012
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This report is public

RECOMMENDATIONS OF COUNCILLOR KAREN LEYTHAM

- (1) That Cabinet adopts in principle a HRA medium term financial strategy and sets a rent policy that supports the future investment needs of the HRA housing stock, and enables the council to consider using HRA funding in a wider regeneration context.
- (2) That Cabinet confirms that it does not intend to meet the rent convergence requirement as recommended by Government.
- (3) That Cabinet approves a medium term rent setting policy with rent increases being capped at no more than 3% per annum.

1 Introduction

- 1.1 The financing of council housing has been centrally directed for many years, through legislation and complex regulations. From 01 April this year council housing became “self-funded” and local authorities are no longer subject to the complexities of the housing subsidy system. Whilst a Housing Revenue Account (HRA) must still be maintained, there is now greater autonomy in setting council housing financial strategy although the Council must still have due regard to various legal requirements - not least the Prudential Code for capital investment.
- 1.2 Prior to self-financing being introduced, local authority rents were predominantly driven by a formula set by the Government, which in turn set a longer term target for rents to reach, although there were limits to the increases allowed in any one year. The council set its rents in line with Government policy to ensure that it could maintain its “Decent Homes” programme and meet its regulatory requirements as a registered provider of social housing, as well as dealing with the annual vagaries of the subsidy system.
- 1.3 Addressing future investment needs and supporting service development within the HRA are inextricably linked to reviewing and establishing its medium term financial strategy, including the rent setting policy. Self-financing has reinforced the need to adopt such a framework, to ensure that the HRA remains financially sustainable in progressing its priorities and objectives.

2 Current Approved Investment Needs

- 2.1 Council housing operates under a statutory regulatory framework. The regulations require that tenants’ homes meet the standard set out in the Government’s Decent Homes Guidance and that the council continues to maintain its homes to at least this standard, or meet the standards of design and quality that applied when the home was built if those standards are higher than the Decent Homes Standard.
- 2.2 The regulations also require the council to meet all applicable statutory requirements that provide for the health and safety of the occupants in their homes.
- 2.3 The first call on council housing finance (HRA) is to meet these requirements and this is reflected in the council’s 30 year HRA Business Plan. Any funding generated is ring-fenced to the HRA and can only be used to invest in or in the creation of HRA assets.
- 2.4 Cabinet set the current budget and capital programme to meet these needs at its 17 January 2012 meeting, and the council has a 5 year approved capital programme to 2016/17 as follows:

Council Housing Capital Expenditure				
2012/13	2013/14	2014/15	2015/16	2016/17
Estimate	Forecast	Forecast	Forecast	Forecast
£3,916,000	£3,616,000	£3,616,000	£3,650,000	£3,960,000

- 2.5 The capital programme is funded from a number of sources: the Major Repairs Reserve, other earmarked reserves, direct revenue financing and capital receipts. The reserve funds are now funded through HRA income, primarily through the rent income from council housing.

3 Future Investment Needs and Opportunities

- 3.1 Self-financing gives the council and its tenants the ability to look at longer term options and opportunities for further investment and growth in its services and stock, which would not have been practical under the previous financial arrangements.

- 3.2 Firstly, a review of the capital programme needs to be undertaken driven by the investment needs of existing housing stock, and evidenced through an updated stock condition survey. The Head of Environmental Services will be undertaking this review.

- 3.3 However, new investment requirements have already been identified in advance of a detailed update of the stock condition:

- Provision for additional fire precaution works £300,000 for first 5 years
- Provision for remodelling of sheltered schemes £100,000 for first 10 years
- Provision for improvements to communal areas to flats £50,000 for first 5 years.
- Increase the boiler replacements from £400,000 per annum to £500,000 per annum.
- Renewable technologies £100,000 for first 5 years.
- Increase the environmental budget from £360,000 per annum to £750,000 per annum.

- 3.4 The above represents a potential increase in the existing capital programme of over £1m per year. These figures still need validating with detailed proposals to be developed.

- 3.5 Secondly, other new investment needs or opportunities should be considered. In the past the council has not been in a position to consider acquisition or new build but the examples given below illustrate the costs of two schemes recently built by housing associations within this district:

Flat development

Total scheme cost £3,367,515 including cost of site 30 units (1 and 2 bedroom flats) so comes in at an average cost of £112,250.50.

General Needs Housing

Total scheme cost £3,533,682 including cost of privately owned site 27 units (7 x 2 bed houses and 20 x 3 bedroom houses) so comes in at an average cost of £130,877.11.

- 3.6 Any increase in the housing stock would not only bring with it additional income but also additional management and maintenance requirements, and these would also need to be factored in to the decision-making.

- 3.7 The use of the council's HRA to facilitate housing regeneration through acquisition or new build will require the setting of a sustainable medium term council housing rent policy to provide the funding. As with the General Fund, any capital expenditure would need to satisfy the requirements of the Prudential Code.
- 3.8 Essentially the council needs to balance its investment needs, opportunities and priorities (be they existing stock improvements or any other potential investment opportunities for increased refurbishment, service investment, regeneration, acquisition and new build), ensuring appropriate tenant/resident input whilst taking a proper long term asset management stance.

4 Current Rent Setting Policy

- 4.1 For local authorities, the Government's current social rent policy provides guidelines for local authority rent increases according to a formula linked to properties. The Government's aim is to ensure that similar properties in the same area will have a similar rent regardless of whether the dwelling is owned by a local authority or a housing association, and that they remain affordable in the future.
- 4.2 Local authorities have existing statutory powers, under section 24 of the Housing Act 1985, to charge reasonable rents.
- 4.3 The Government is still seeking to influence local rent policy and is still proposing to issue annual guidance.
- 4.4 Cabinet of 17 January 2012 resolved that future year budget projections be set in line with the national social rent restructuring policy with average rent increases of 4.64% for 2013/14 and 4.61% for 2014/15.
- 4.5 It was also reported then, however, that rent increase assumptions for 2013/14 onwards would be reviewed again in future years' budget processes. Following the implementation of the self-financing regime, there is now better scope to consider amending the HRA rent setting policy for future years.

5 Future Rent Setting and Investment Capacity

- 5.1 In considering options the council is required to ensure the longer term financial viability of the HRA and delivery of its 30 year business plan, together with the service outcomes required by the regulatory framework that the service operates within. The financing of council housing is now driven by the rental income stream, and the rents set by the council.
- 5.2 In terms of the key financial issues stemming from self-financing, the message given by the council's independent financial advisors was that:
- Early years (1-5)
Debt repayment can be covered.
 - Medium term (years 5-7)
Increased programme required and able to be funded but is

6.2 The following two tables show alternative rent increases and their resulting annual increase or decrease in available reserves.

Alternative rent increases:

		2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
Annual Percentage Increase	1%	£69.91	£70.61	£71.32	£72.03	£72.75	£73.48	£74.21
	2%	£70.60	£72.01	£73.45	£74.92	£76.42	£77.95	£79.51
	3%	£71.30	£73.44	£75.64	£77.91	£80.25	£82.66	£85.14
	4%	£71.99	£74.87	£77.86	£80.98	£84.22	£87.59	£91.09
	5%	£72.68	£76.31	£80.13	£84.14	£88.34	£92.76	£97.40
	6%	£73.37	£77.77	£82.44	£87.38	£92.63	£98.19	£104.08

Shaded Areas Exceed Formula Rent

6.3 The available balances resulting from alternative rent increases are shown below and are compared to the balances available from the current Business Plan assumptions. It is important to note at this point that the current level of available reserves as at 01 April 2012 stands at £7.856M in the Major Repairs Reserve and Unallocated HRA Balance – the minimum level of unallocated balances is currently set at £350K.

		Cumulative Reserve Balances							Cumulative Balance as at Year 30 2041/42	
		2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	
		£000	£000	£000	£000	£000	£000	£000	£000	£000
Current Projections		9,661	10,128	11,135	12,467	13,744	13,101	13,125	15,699	111,319
Annual Percentage Increase	0%	9,661	9,507	9,248	8,668	7,593	4,137	863	(346)	(147,258)
	1%	9,661	9,642	9,653	9,473	8,930	6,139	3,664	3,388	(86,842)
	2%	9,661	9,777	10,061	10,290	10,296	8,197	6,561	7,276	(13,826)
	3%	9,661	9,912	10,471	11,118	11,690	10,312	9,559	11,326	79,153
	4%	9,661	10,047	10,885	11,957	13,111	12,476	12,542	15,211	138,696
	5%	9,661	10,182	11,302	12,703	14,145	13,776	14,174	17,246	186,751
6%	9,661	10,317	11,620	13,169	14,815	14,719	15,461	18,957	244,601	

Shaded Areas Exceed Formula Rent

6.4 The above provides a very simplistic view on how reserves change with different rent increases. This shows that if an annual rent increase of less than 3% was applied then there would be insufficient reserves to finance the overall 30 year business plan as reserves would be negative, as set out in the final column. In addition annual increases above 3% would eventually exceed the formula rent and may well have implications for housing benefit subsidy limitation.

6.5 However, in all likelihood circumstances will change year on year and the

following table shows how different annual increases can still generate sufficient reserves to maintain the business plan.

	Cumulative Reserve Balances								Cumulative Balance as at Year 30 2041/42
	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	£000
Current Projections	£000	£000	£000	£000	£000	£000	£000	£000	£000
	9,661	10,128	11,135	12,467	13,744	13,101	13,125	15,699	111,319
0%,1%,2%,3% thereafter	9,661	9,506	9,381	9,195	8,909	6,649	4,988	5,822	41,369
1%,2%,3% thereafter	9,661	9,641	9,788	10,010	10,145	8,317	7,102	8,394	59,559
2%,3% thereafter	9,661	9,776	10,197	10,701	11,126	9,597	8,689	10,296	72,485
3%	9,661	9,912	10,471	11,118	11,690	10,312	9,559	11,326	79,153

6.6 As previously mentioned, the above projections are based on the latest 30 year business plan, which in turn is based on the previous stock condition survey. Undoubtedly the projections will change again when the stock condition survey is updated following the review by the Head of Environmental Services. That being said, the items referred to in paragraph 3.3 have already been incorporated as well as indicative estimates for the impact of the welfare reforms. The projections are therefore considered to be a reasonable basis on which to consider future rent policy, subject to regular review.

7 Options: Future Rent Setting Policy

7.1 The council needs to decide whether it wishes to achieve rent convergence, as assumed by the Government, or whether it wishes to set alternative rent objectives.

7.2 If the council chose to move away from the Government's social rent policy of convergence, the amount of future funding available within reserves would decrease as illustrated above.

7.3 In addition, as highlighted, there may be new or greater risks to the income available particularly through the impact of future welfare reforms, and this will affect financial and investment planning. In particular there may be a need to increase the minimum level of HRA balances held.

7.4 It is recommended, therefore, that the council establishes a stable method of determining the annual review of rent.

7.5 Possible options:

- **Option 1:**
To continue to follow the Government's social rent policy including convergence factors (Actual rents are increased by RPI +0.5% plus (an amount equal to the difference between the guideline rent and the actual rent) divided by the number of years remaining to convergence. This was subject to a maximum capped increase of RPI+ 0.5% + £2 in order that

rents are not subject to extremely high rent increases)

- **Option 2:**
To continue to follow the Government's social rent policy excluding convergence factors (Actual rents are increased by RPI +0.5%)
- **Option 3:**
To establish a local social rent setting policy that supports the future investment needs of the Housing Revenue Account, drawing on the annual rent increase scenarios outlined earlier.

	Option 1: To continue to follow the Government's social rent policy including convergence	Option 2: To continue to follow the Government's social rent policy excluding convergence factors	Option 3: To establish a local social rent setting policy adopting the medium term financial strategy and principles set out in the report
Advantages	<ul style="list-style-type: none"> • The Government's objectives of convergence are met. • Maximises the amount of money available to invest in new services and assets • Rents remain affordable and the housing benefit cost are met by Government 	<ul style="list-style-type: none"> • Rent increases are still linked to RPI • Money available to invest in new services and assets • Rents remain affordable and the housing benefit cost are met by Government • Reduced pressure on individual tenants' budgets 	<ul style="list-style-type: none"> • The council establishes a stable and sustainable budget capable of withstanding financial pressures • Rent is set in the local context to provide the financial resources needed to deliver the council's HRA priority outcomes • Money available to invest in new services and assets • Rents remain affordable and the housing benefit cost are met by Government • Reduced pressure on individual tenants' budgets

	Option 1: To continue to follow the Government's social rent policy including convergence	Option 2: To continue to follow the Government's social rent policy excluding convergence factors	Option 3: To establish a local social rent setting policy adopting the medium term financial strategy and principles set out in the report
Disadvantages	<ul style="list-style-type: none"> • Rent levels not locally set in response to the financial resources needed to deliver the council's HRA priority outcomes • Increase pressure on tenants' individual budgets 	<ul style="list-style-type: none"> • The Government's policy on rent convergence is not delivered. • Rents are not increased above RPI by the Government formula to achieve convergence with Private registered Provider Social rents • The rent levels between comparable properties will remain different across social housing landlords within the district • Lower amount of money available to meet existing or future needs 	<ul style="list-style-type: none"> • The Government's policy on rent convergence is not delivered • Rents are not increased by the Government formula to achieve convergence with Private registered Provider Social rents • The rent levels between comparable properties will remain different across social housing landlords within the district

	Option 1: To continue to follow the Government's social rent policy including convergence	Option 2: To continue to follow the Government's social rent policy excluding convergence factors	Option 3: To establish a local social rent setting policy adopting the medium term financial strategy and principles set out in the report
Risks	Future rent levels may not fit with local spending and investment needs.	Future rent levels may not fit with local spending and investment needs.	<ul style="list-style-type: none"> • Insufficient funding generated to meet the investment needs of the HRA if rent levels set too low. • If rent level set too high formula rent and limit rent may be exceeded with implications for housing benefit subsidy limitation (until universal credit is implemented, which could raise other issues for any option).

8 Adopting a Medium Term Financial Strategy for the HRA

8.1 The main objectives of any HRA Medium Term Financial Strategy would be to:

- Explain the financial context within which the council's HRA is set to work over the medium term.
- Provide a medium term forecast of resources and expenditure.
- Identify the financial resources and target rent levels needed to deliver the council's HRA priority outcomes and its rent setting policy.
- Identify any budgetary savings / efficiency targets.
- Provide a framework for due consideration, comparison and prioritisation of competing spending and investment needs.
- Achieve a stable, affordable and sustainable budget capable of withstanding financial pressures.
- Keep the above updated, setting out a clear process for regular monitoring and review.

- 8.2 Given the challenges and risks, the following principles should underpin any medium term financial strategy adopted:
- Continue to ensure that the Decent Homes standard and local standards are maintained.
 - Support any other specific HRA priority outcomes as adopted.
 - Inform and support the adopted rent setting policy.
 - Maintain balances, earmarked reserves and provisions at prudent levels.
 - Continue to strive for greater efficiencies from within the HRA.
- 8.3 In essence, the HRA MTFFS would draw together all the key strategic financial aspects for the council housing service, to help inform its future direction.
- 8.4 It is proposed that the council adopts in principle a HRA medium term financial strategy, to provide a stronger financial planning framework in support of the Council's legal and regulatory requirements as a registered provider of social housing. If Cabinet approves this approach, the detailed content of the draft HRA MTFFS would be brought back for Member approval.
- 8.5 The development of such a strategy would incorporate sufficient flexibility to enable the council to look beyond the needs of the existing stock, facilitating the consideration of stock replacement through acquisition or new build as well as the HRA's contribution in a wider housing regeneration context. This would involve measures such as establishing an Investment Reserve Fund separate to the existing Major Repairs Reserve. The extent of the funds available in reserves would be very much dependent on the rent setting strategy adopted.
- 8.6 To support the development of any medium term financial strategy, therefore, firstly the council would need to establish its rent setting policy and associated targets.
- 8.7 **Possible Options:**

HRA Medium Term Financial Strategy Options Summary

	Option 1: To adopt a HRA medium term financial strategy underpinned by the principles set out in the report	Option 2: Do not to adopt a HRA medium term financial strategy
Advantages	<ul style="list-style-type: none"> • The council has a financial context within which the council' HRA is set to work over the medium term • The council identifies the financial resources needed to deliver the council's HRA priority outcomes • The council has a medium term forecast of resources and expenditure • The council establishes a stable and sustainable budget capable of withstanding financial pressures 	None

Disadvantages	None	<ul style="list-style-type: none"> • The council will not have a framework on which to base its financial decisions relating to the HRA • A short term approach to budgeting and rent setting would continue.
Risks	Financial and other forecasts underpinning any MTFs prove unsound – this risk would be managed through monitoring and review processes.	Financial risks are not managed nor controlled in a strategic context - the council may not have sufficient funds to meet the revenue or capital needs of the HRA, surpluses could arise for which there is no clear purpose, or rent increases could fluctuate unnecessarily.

9 Details of Consultation

Discussions have taken place within the Housing and Regeneration Cabinet Liaison Group and with the District-wide Tenants Forum about the need to establish a HRA the medium term financial strategy and rent setting policy and there was a general consensus around the approach and principles as set out in this report.

10 Officer Preferred Option (and comments)

10.1 Rent Setting Policy

10.1.1 The options analysis shows that all options provide for a sustainable HRA and provide headroom for investment in service improvements and increasing the housing stock. All the options ensure that the currently identified service and investment needs are met, subject to the principles underpinning any medium term financial strategy being adhered to and no major unforeseen matters arising.

10.1.2 Option 1 of continuing to follow the Government's social rent policy would ensure that social rent levels between comparable properties across social housing landlords within the district become the same. The greatest amount of investment headroom is expected. Rents would still remain comparatively affordable.

10.1.3 Option 2 would result in rent levels between comparable properties remaining different across social housing landlords within the district but would produce a lower rent increase for tenants. The amount available for additional investment would be less than under Option 1.

10.1.4 Option 3 would ensure that the council sets its rents to provide the financial resources needed to deliver the council's HRA priority outcomes. Again it would result in rent levels between comparable properties remaining different

across social housing landlords within the district, but is expected to produce a lower rent increase for tenants. The amount available of additional investment is also expected to be lower than under Options 1 and 2, depending on what level of increase is actually set.

- 10.1.5 The requirement on the council is to ensure that the HRA remains viable and sustainable, and provides the financial resources needed to deliver the council's HRA priority outcomes. Ultimately, if Council wishes to provide for the widest investment opportunities, then Option 1 is considered most appropriate. If a lower level of investment is acceptable, however, Option 3 may be more appropriate and if so, Cabinet is requested to indicate its preferred annual percentage increase. Whatever rent setting policy route is chosen, it will be subject to regular review, thereby giving the opportunity to respond to changing circumstances.

11 HRA Medium Term Financial Strategy

- 11.1 With Option 1 the council could ensure that it has a financial context within which the HRA could work over the medium term, identifying the financial resources needed to deliver the council's HRA priority outcomes and providing a medium term forecast of resources and expenditure.

12 Conclusion

- 12.1 Should Members choose to adopt a HRA medium term financial strategy and rent policy underpinned by the principles set out in the report, it would help ensure that sufficient funding is available to meet the present and future needs of the HRA housing stock. In addition the council would be able to look beyond the needs of the existing stock and consider stock replacement through acquisition or new build, and to also consider its housing contribution in a wider housing regeneration context.

RELATIONSHIP TO POLICY FRAMEWORK

The proposals support the objectives and resource management framework set out in the Corporate Plan.

CONCLUSION OF IMPACT ASSESSMENT

(including Diversity, Human Rights, Community Safety, Sustainability and Rural Proofing)

No significant implications directly arising.

LEGAL IMPLICATIONS

Local authorities have existing statutory powers, under section 24 of the Housing Act 1985, to charge reasonable rents. The Government has recently confirmed that the rental policy statements issues, normally in late December, have the status of non-statutory guidance. Authorities have the flexibility to set rents at another level, or using another basis, if that appears to them more appropriate to local circumstances.

FINANCIAL IMPLICATIONS

These are contained within the body of the report.

SECTION 151 OFFICER'S COMMENTS

The adoption of a MTFS / rent policy for council housing would promote sounder financial planning for the HRA, particularly now that self-financing has been implemented. In due course the exact narrative for this element of the MTFS would also be presented to Members – the specific decision-making arrangements would also need setting out at that time too (the Council's existing MTFS is part of the policy framework and is therefore a matter for Council, whilst rent setting is an executive function and still rests with Cabinet.)

MONITORING OFFICER'S COMMENTS

The Monitoring Officer has been consulted and has no further comments.

BACKGROUND PAPERS

Policy Framework for Setting Social Rents and Service Charges (Lancaster City Council)

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