Havering
LONDON BOROUGH

REPORT OF THE CABINET

THE REFORM OF COUNCIL HOUSING FINANCE (IMPLEMENTATION)

The Government is implementing a scheme which will bring the Housing Subsidy system to an end in April 2012. The enabling legislation is included within the Localism Bill, which is due to pass into law in December 2011. What is proposed in effect is that local authorities would get the independence and responsibility for the management of their housing stock that they are seeking, but this would be in return for a "payment" which represents the redistribution of the national housing debt in the form of a one off payment to or from Central Government. For Havering Council, this would be a payment to the Government given that the Council is already in negative subsidy, that is, it pays into the national HRA subsidy each year under the current arrangements. The national balance of these individual payments for and to housing authorities represents some part of the future surpluses that the Government had anticipated it would have received had the system continued in its present form.

Cabinet received a report in October 2011 which presented information about the proposed new Housing Revenue Account System which is due to be implemented in April 2012. Under the new system, it is currently projected to require the London Borough of Havering to take on estimated additional housing debt of £160m, which will mean that the Council's total housing debt will be £203m. These estimates are subject to changes before the final figures are known in January 2012. It was reported that the Council would have to manage this debt and deliver a decent level of stock investment over a 30 year HRA Business Plan. The initial baseline HRA Business Plan model presented to Cabinet showed that this is achievable as long as the Decent Homes funding allocated in February 2011 remains in place.

Cabinet endorsed the baseline HRA Business Plan Model (as set out in the Appendix to this report) for the management of the Council Housing stock over the next 30 years and the assumptions that were included in it. It also committed to carrying out an annual review of the HRA Business Plan, in order to ensure that the objectives of maintaining the condition of the Council's housing stock and meeting the Council's financial obligations were fulfilled.

RECOMMENDATION:

That Council approve the baseline HRA Business Plan model

The Baseline HRA Business Plan Model APPENDIX

The first set of financial models that have been constructed look at what would happen if the current system continued in the present form. This would result in a very difficult position for the Council over the forthcoming years. The stock investment work that is required would never be completed; the level of housing debt would never be paid off, and the HRA would quickly go into deficit and end up at a negative figure of minus £50m by Year 30 if no action was taken to drastically reduce costs. This is illustrated at Appendix 1.

*Under the Self Financing regime, there is a better future in prospect, although of course there are risks associated with this regime that need to be taken into account. A **baseline HRA Business Plan model** has been drawn up. It should be noted that given that the final debt figures are yet to be released by the Government, the work to date should be considered a baseline model, rather than a finalised opening HRA Business Plan. Housing, Homes in Havering and Finance officers have worked together to establish a series of prudent assumptions for baseline HRA Business Plan model, which are as follows:*

- *RPI at 2.5% through the life of the plan*
- *financing costs at 6.0% through the life of the plan*
- *13 properties sold through the Right to Buy each year throughout the life of the HRA Business Plan (which is the current level of disposals)*
- *the stock investment requirement is that identified in the Stock Condition Survey (which is more than is required under Decent Homes, though not beyond a 'mortgageable' level for the properties)*
- *balances in the HRA need to be maintained at a minimum provision of £2m*
- *Right to Buy receipts are not used for housing purposes up to the level of anticipated sales*
- *Decent Homes funding is provided by the Government as allocated in February 2011 (£62.7m over four years)*
- *voids level at 1.4% and bad debt at 0.76%*
- *opening number of properties 9,959, with an average rent of £74.92*
- *opening debt of £203.097m (net additional debt of £160.342m). It should be noted that should the new RPI rate of 4.5% would increase the total debt figure by £6.5m.*

The baseline HRA Business Plan model is illustrated at Appendix 2. Under the model, balances can be maintained at the minimum required level, whilst the work is carried out. The baseline HRA Business Plan model shows that the backlog of work is completed in Year 12, and thereafter the balances begin to rise which enables the Council to pay of its debt by Year 24, if it chooses to do so. It should be noted that completing all the backlog of stock investment within 12 years, may not be readily acceptable to tenants, however, it should be noted that decent homes investment will be completed by year 8 at the latest. The Government *requires that for councils with non-decent stock, the HRA Business Plan must deliver the last 10% of non-decency through its own resources. Also, there is the added pressure of newly arising non-decency. That said, through prioritisation of decency above other investment, decency could be delivered before year 8 if desirable.*

A number of alternative assumptions and scenarios have been applied to the baseline HRA Business Plan model so as to test the impact of a range of actions and approaches to planning for the housing stock over a 30 year HRA Business Plan. The scenarios are set out below in Table 1, and the summary of the impact is shown in Table 2.

There are in fact an infinite number of alternative scenarios that could be examined, and it is likely that over time as the HRA Business Plan is reviewed and tested, a mix of factors will pertain. For example, in the examples in the table, it is assumed that either no or all the RTB receipts are applied to Housing, but it is of course possible to apply different proportions in the HRA Business Plan and assess the impact.

SCENARIO		HRA Surplus Point (>£2m) Year	SCS Investment Backlog cleared Year	Debt Free Point Year
	Baseline HRA Business Plan model	24	12	24
Variants to the baseline HRA Business Plan model				
1	RPI = 4% rather than 2.5%	21	11	21
2	Inflation on capital 1% > RPI	28	16	28
3	Inflation on capital 2% > RPI for first 10 years	29	20	29
4	Interest Rate 7% compared with current assumption of 6%	27	17	26
5	RTB sales rise to 50 instead of 13 per annum	27	14	27
6	Right to Buy receipts are applied to the HRA Business Plan	24	11	23
7	No real ½% inflation on rents	30	18	30
8	Reduce level of investment to minimum Decent Homes Level	20	8	20
9	Debt settlement figure £6.25m higher (possible 2012/13 settlement figure)	25	13	25
10	No real ½% inflation on rents Interest Rate 7% compared with 6%	30+	26	30+
11	No real ½% inflation on rents Interest Rate 7% compared with 6% Invest Decent Homes Level	30+	23	30+
12	No real ½% inflation on rents Inflation on capital 1% > RPI	30+	27	30+
13	Interest Rate 7% compared with 6% Inflation on capital 1% > RPI	30	23	30
14	Interest Rate 7% compared with 6% Inflation on capital 1% > RPI; Invest Decent Homes Level	29	21	29

The scenario testing when applied to the baseline HRA Business Plan model and displayed in the above table indicates that the most significant factors that make a difference to the HRA Business Plan are:

- *the level of financing costs, and whether it rises significantly above 6%*
- *the level of investment carried out, and*
- *capital inflation.*

It then becomes a question in planning the way forward, how long it is considered acceptable for tenants to have the work programme completed; and what level of stock investment is acceptable.

There are clearly some major risks associated with this HRA Business Plan. For example, it is clear that one of the risks that cause major difficulties is a long and consistent period of high capital inflation. Should this occur, then it would be necessary for the Council to take action to mitigate the risk. This might be either to cut the investment programme for a period, or to inject some additional resources, such as capital receipts.

A second risk is the risk of interest rates rising. This is clearly a risk that is quite likely to occur, and the action that might be available to mitigate this risk, is to adopt a range of borrowing tactics, including some long term fixed rate borrowing, to introduce a level of certainty in the HRA Business Planning. What will be different in the future, under a HRA Business Plan, is that the Council will be adopting real business planning, managing these risks pro-actively and making real decisions about rents, investment, borrowing and payment of debt. The Council has appointed financial advisors, Sector Housing Services, to carry out the initial assistance in preparing for Self Financing, but regular ongoing advice will need to be tendered in order to establish a regular review of the HRA Business Plan.

<u>Disposals and demolitions</u>

One of the key factors influencing the level of debt that the Council will be obliged to take on is the number of properties that we have; the fewer the properties, the lower the level of debt the Government calculates that the HRA Business Plan can support. The guidance regarding the opening debt settlement allows the Council to disregard from its opening stock level any properties it plans to demolish before March 2017, so long as the Council has resolved to demolish the properties and has consulted all the tenants involved and this has been verified by the Council external auditors by no later than 10 October 2011. These requirements have been met and so the necessary audit sign off of all planned demolitions has been granted. Therefore, the Council can be sure that the benefit of its current demolition plans will be reflected in its opening debt settlement. The opening number of housing dwellings within the HRA Business Plan will be around 9,959.

If and when, in the future, the Council wishes to consider any proposals for disposal / demolition, it remains an option for the Council to manage its stock actively, and make future disposals and/or demolitions if it chooses to do so. However, the calculation of the financial effect on the HRA Business Plan needs to include consideration of the impact of the loss of income (and loss of repairing and investment responsibilities) of *each disposal, and a decision will need to be made in relation to that impact at that point in the lifetime of the HRA Business Plan.*

Stock Investment level

The Council has an obligation as a landlord to maintain its properties. In addition there is a Government target to eliminate the backlog of investment in social housing, and achieve the Decent Homes standard. This obligation has been funded through the Backlog Funding scheme, and Havering Council is due to receive a total of £62.7m over the four years 2011/12 to 2014/15 to complete 90% of our Decent Homes work.

The Decent Homes Standard however, does not include a number of significant items that would maintain our housing stock at a mortgageable standard. These include, for example, lift repairs and environmental works. The level of investment included in the baseline HRA Business Plan model therefore includes those essential works that would achieve this higher level of stock quality. This level is achievable within the current baseline HRA Business Plan model. An alternative scenario which would see completion of the minimum Decent Homes Standard is included as Scenario 8 in the table under paragraph 4.5 above. This shows that should this lower level of investment be carried out, then the work would be completed by Year 8 and the debt be paid off by Year 20.

The level of investment that has been included in the baseline HRA Business Plan model is therefore Decent Homes as a base plus additional works that would ensure that the property is mortgageable. This means that the property maintains in effect its market value, and can be bought and sold as required. For example, our properties that are system built properties under certain designated non traditional methods used immediately after the war cannot be sold on the open market, as there are no lenders willing to provide mortgage funds to buy them. The work that is included in the stock investment programme will bring them up to a standard that will enable them to be sold on the open market. Should we fail to maintain a programme of maintenance of our stock, we would be obliged to set aside greater sums to provide for depreciation of our assets.

It is recognised that there is difference between the level of borrowing the Council needs to take on to make the payment to the Government under the opening debt settlement, and the cap on the maximum amount the Government would allow the Council to borrow for self-financing purposes. This is commonly referred to as the 'headroom' within the self-financing regime. It should be noted that the Government has set this upper limit for Havering at an estimated £27m above the figure required to pay off the debt. In effect this means that the Council may, if it chooses to do so, borrow additional money, but only for the purposes of implementing Self Financing and investment in its housing.

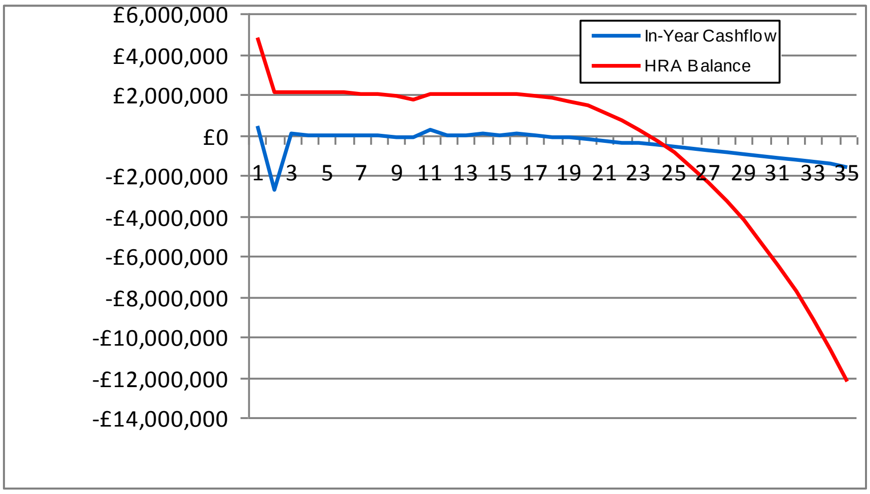
At this stage, it is proposed that no additional borrowing should be undertaken as it is recognised that this headroom is not immediately required to bring the stock up to the Decent Homes and mortgageable standard within a reasonable timescale. It is also recognised, however, that there are considerable additional pressures for further housing stock investment that are likely to arise over the coming 30 years, which may also give rise to additional expenditure.

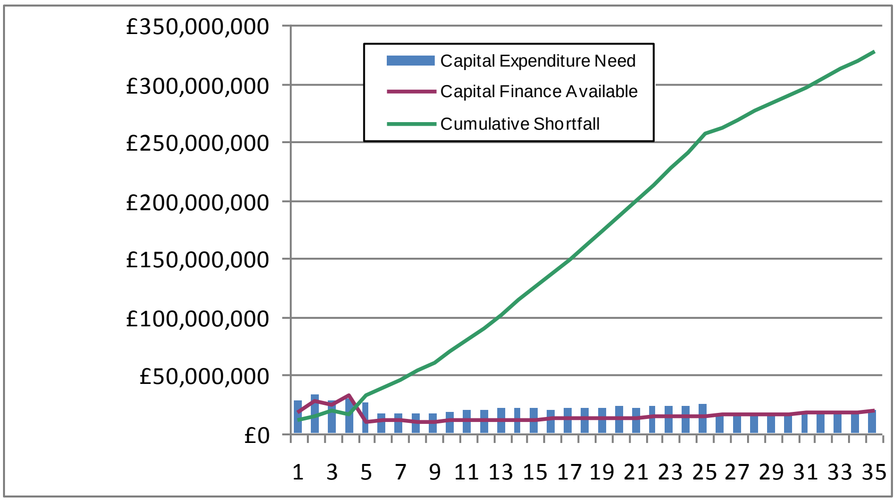
It is prudent to retain the need for additional housing investment funded from headroom borrowing under constant review. Maintaining the sustainability of the Council's stock and estates in coming years could require additional investment. For example, standards relating to fire risk mitigation, legionella, asbestos remediation, and electrical safety are constantly rising and so could lead to additional investment needs. Furthermore, there may be additional option work that tenants and members would wish to bring forward to improve the quality of the housing stock. Some works which are optional and not included in the current baseline HRA Business Plan model that may arise over the next 30 years include:

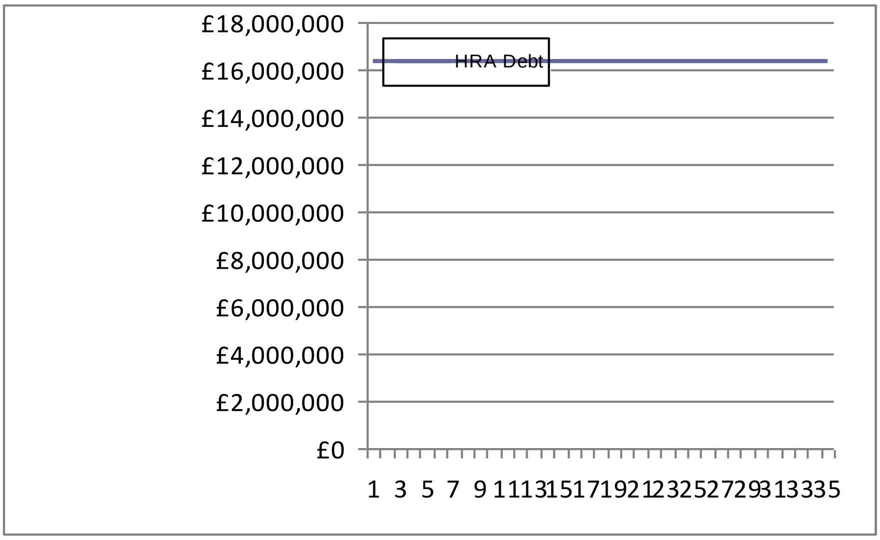
Housing affected	*Item*
Sheltered housing	*Some sheltered housing does not have lifts, and as existing residents age, they have either to move, or their independence is restricted. It may be helpful to have a programme to install lifts*
	As the resident population ages, it is helpful to change the balance between sheltered accommodation and extra care accommodation which enable a frailer group of residents to remain independent. More of these units can be converted to extra care, rather than independent sheltered accommodation
	Telecare equipment can be installed and upgraded within sheltered accommodation in order to maintain the independence of existing residents
Energy efficiency	*The properties most difficult to insulate, are solid brick construction dwellings. A programme of external insulation to these properties will assist with the Council's commitment to energy efficiency*
	Solar PV panels. Plans are advanced to start a programme to install Solar PV panels. This programme could be accelerated
Car Parking	*There has been a programme to remove redundant garages across housing estates, but it has also left a legacy of some additional requirement for remodelling off street parking in order to accommodate increasing car ownership*
Estate improvements	*There are continuing problems with some communal areas on estates, which need estate improvements, play areas, gating of alleys, and improved paths and fencing*
Provision of new accommodation, such as bungalows	*There is a programme of assisting elderly tenants who are under occupying their homes, but who are reluctant to move the Council does not have accommodation of the quality that they would be willing to accept. A programme to provide some high quality one and two bed bungalows in locations which are acceptable may be a solution to this.*
Other basic improvements	*There are problems with the need to improve continuously sound insulation, fire prevention measures, communal areas such as lobbies and lift areas, shops and community centres*

Investment requirements in these, or other areas, need to be kept under review and it is prudent to retain the option to using the headroom borrowing to meet needs as they arise.

Appendix 1 – HRA projection under the existing HRA subsidy system







Appendix 2 – Baseline HRA Business Plan model

Assumptions

- *RPI at 2.5% through the life of the plan.*
- *Financing costs at 6.0% through the life of the plan.*
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- *The stock investment requirement is that identified in the Stock Condition Survey (which is more than is required under Decent Homes, though not beyond a 'mortgageable' level for the properties).*
- *Balances in the HRA need to be maintained at a minimum provision of £2m.*
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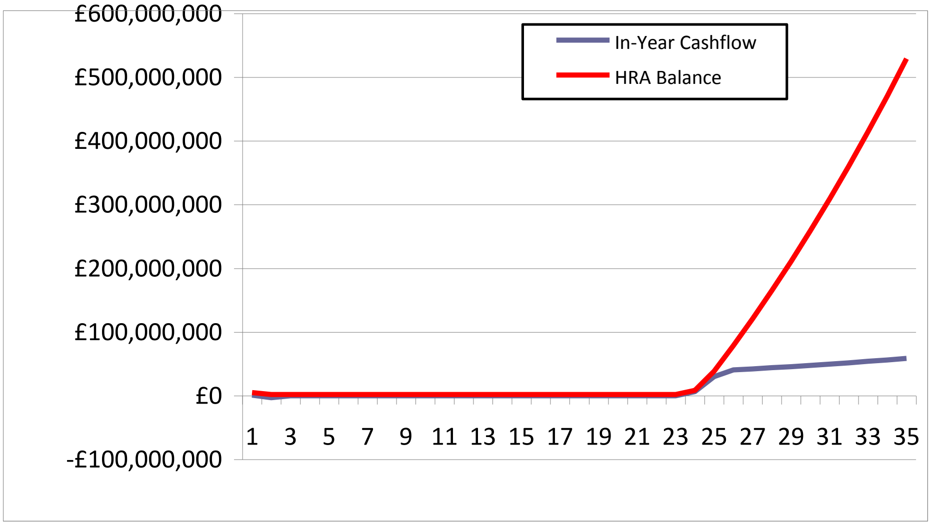
- *Voids level at 1.4% and bad debt at 0.76%.*
- *Opening number of properties 9,959, with an average rent of £74.92.*
- *Opening debt of £203.097m (net additional debt of £160,342m). It should be noted that should the new RPI rate of 4.5% would increase the total debt figure by £6.5m.*

Summary of Outcomes

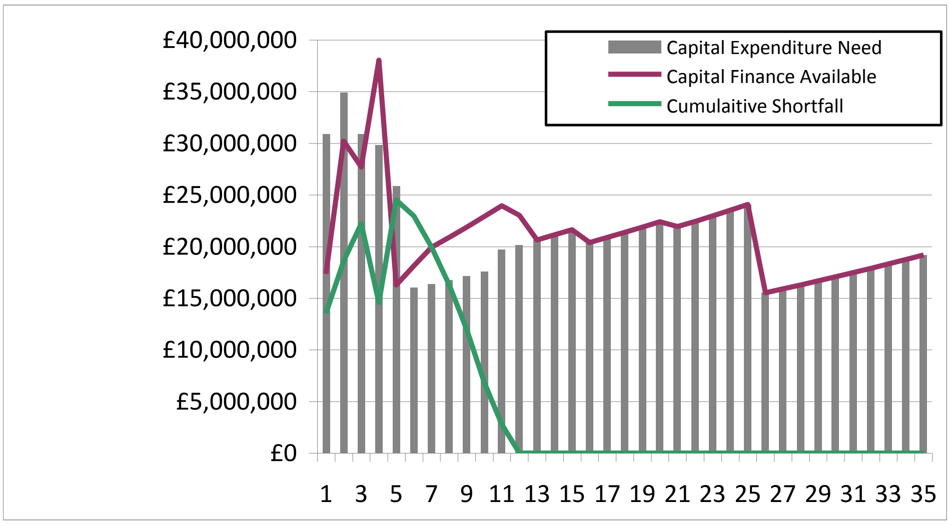
- *HRA surplus point (>£2m) achieved in year 24 of the 30 year plan.*
- *Stock Condition Survey investment backlog cleared in year 12.*
- *Debt free point achieved in year 24.*

HRA Balances

Council, 23 November 2011



Investment profile



Debt profile