**Manchester City Council**
**Report for Information**

**Report To:** Resources and Governance Scrutiny – 6 December 2022

**Subject:** Housing Revenue Account 2023/24 to 2025/26

**Report of:** Strategic Director (Development)
Strategic Director (Neighbourhoods)
Deputy Chief Executive and City Treasurer

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**Summary**

This report presents members with an update on the ongoing work being undertaken to finalise the 2023/24 Housing Revenue Account (HRA) budget, the final proposed budget will be brought back to Members in March as part of the overall Council budget approvals.

Given the current economic climate and the cost of living pressures faced by tenants this report sets out the current assumptions for the 2023/24 HRA budget, and the impact of the proposals on both the HRA and tenants. Social rents have been subjected to annual increases aligned to a national rent policy, and this would allow social housing rents to be increased by up to the consumer price index (CPI) plus 1%, this would mean that next year’s rents would be increased by 11.1%. The Government did undertake a consultation exercise around what the rent cap should be set at next year, following the conclusion of consultation Government have now advised that that the maximum social rent increase should be capped at 7%.


**Recommendations**

The Committee is recommended to consider and comment on the approach and assumptions used in preparing the Housing Revenue Account Budget.

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**Wards Affected:** Ancoats & Beswick, Charlestown, Cheetham, Crumpsall, Harphurhey, Higher Blackley, Moston, Ardwick, Clayton & Openshaw, Miles Platting & Newton Heath and Piccadilly

| **Environmental Impact Assessment** - the impact of the issues addressed in this report on achieving the zero-carbon target for the city |
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| As part of developing the HRA capital programme the retrofitting of existing homes to meet zero carbon objectives is at the heart of the programme. |

| **Equality, Diversity and Inclusion** - the impact of the issues addressed in this report in meeting our Public Sector Equality Duty and broader equality commitments |
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| Consideration has been given to how the proposals in the HRA budget could impact on different protected or disadvantaged groups. Where applicable proposals will be subject to completion of an Equality Impact Assessment (EqIA). |

| Manchester Strategy outcomes | Summary of how this report aligns to the OMS/Contribution to the Strategy |
|---|---|
| A thriving and sustainable city: supporting a diverse and distinctive economy that creates jobs and opportunities | A healthy and fit for purpose affordable housing market will support a functioning local and sub regional economy. |
| A highly skilled city: world class and home grown talent sustaining the city's economic success | Access to appropriate affordable housing and services will support residents to achieve and contribute to the city. |
| A progressive and equitable city: making a positive contribution by unlocking the potential of our communities | The supply of affordable good quality homes will provide the opportunity for Manchester residents to raise their individual and collective aspirations. |
| A liveable and low carbon city: a destination of choice to live, visit, work | The right mix of affordable quality energy efficient housing is needed to support growth and ensure that our growing population can live and work in the City and enjoy a good quality of life. |
| A connected city: world class infrastructure and connectivity to drive growth | Affordable social housing plays an important part in ensuring that there are neighbourhoods where people will choose to live, and their housing needs and aspirations are met. |

Full details are in the body of the report, along with any implications for:

- Equal Opportunities Policy
- Risk Management
- Legal Considerations

**Financial Consequences – Revenue**

All expenditure and income related to the provision of Council housing must be contained within the Housing Revenue Account which is a ring-fenced budget separate to the Council's General Fund. Whilst HRA expenditure can exceed income in any given year, this deficit must be covered from reserves and the HRA cannot go into deficit overall. Work is ongoing to prepare the HRA 2023/24 budget and the full budget will be brought back to members in February for final approval. It should be noted that the HRA budget is in balance in the short medium term, and although there is a forecast deficit of c£47m over the 30-year period, the longer-term model is sensitive to cumulative changes and any relatively small change in year 1 will have a much larger impact over the life of the business plan. Notwithstanding this, officers are continuing to look at all budgets in order to ensure that all spending is in line with agreed objectives, and that all spending represents value for money, and this will help ensure a balanced budget over the life of the business plan.

The HRA financial plan covers a rolling period of 30 years and considers all rental incomes, Private Finance Initiative (PFI) grants and heating charges, which must be used for the purpose of funding the costs of managing and maintaining HRA assets.

**Financial Consequences – Capital**

Within the proposed HRA budget a mandatory charge for depreciation is made, and this can be used to either fund capital expenditure or reduce housing debt. In the current years HRA, depreciation if forecast to be c£19m, and the capital programme is forecast to spend c£41.6m.

The current approved programme of capital expenditure for the financial years 2023/24- 2025/26 is for approximately £137.4m of spend, of which c.£12.4m will be funded from grants. Work is ongoing to review the capital programme to ensure that the programme is both deliverable and affordable whilst aligning with Council priorities. The approved programme does include some schemes that will support the Council in becoming carbon neutral by 2038.

From 2025/26 onwards the HRA budget includes an annual capital budget of c£23m per annum which increases annually in line with CPI.

Officers are developing the asset management plan, and this will inform the future capital programme and investment plan for our housing stock. This will need to address important issues including ensuring decent homes standards are achieved and maintained, and carbon reduction and fuel poverty are addressed.

The HRA capital budget already allows for the costs and implications of the following new build programmes: -

- Silk Street (69 properties) (2023-24)
- Collyhurst (130 properties) (20024-25 and 2025-26)

The 30-year business plan factors in the income and costs associated with these new properties entering the portfolio once completed.

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**Background documents (available for public inspection):**

None.

## 1. Introduction

1.1 The purpose of this report is to update committee around the ongoing work in preparing the 2023/24 Housing Revenue Account (HRA) budget, this includes setting out the assumptions that are being made as part of the budget and the implications of setting a rent cap on both the HRA business plan, and for tenants.

## 2. Statutory Duties in Determining the HRA Budget Strategy

2.1 The rules governing the maintenance of the HRA were established pursuant to the Local Government and Housing Act 1989 and provide that:

- The Council must formulate proposals in respect of HRA income and expenditure for the financial year which, on the best assumptions and estimates that the Council is able to make at the time, ensure that the HRA does not show a deficit balance.
- The Council is required to keep a HRA in accordance with proper practice. The Council has the responsibility to determine a strategy that is designed to ensure that the HRA is in balance over the course of the business plan.
- The HRA continues to be a ring-fenced account, this means that it must, in general, balance on a year-to-year basis, so that the costs of running the Housing Service, which include debt charges, administration costs, maintenance expenditure and PFI charges must be met from HRA income.

2.2 The ringfencing of the HRA needs to ensure that all the income and expenditure in relation to managing of the council housing stock is separate to the General Fund and that there is no cross subsidy between either fund.

## 3. Background

3.1 Since the introduction of Self Financing within the HRA from April 2012 the Council has had to manage its housing stock on a similar basis to other Registered Providers of social housing. This has entailed developing a rolling 30-year business plan and reviewing the use of existing assets to ensure that benefits are maximised.

3.2 The HRA includes the following components:

- Income and expenditure, including staffing costs, repairs & maintenance other operating costs and capital investment for council owned stock, formerly Northwards Housing
- The Private Finance Initiative Contracts (PFI) costs for Plymouth Grove, Miles Platting and Brunswick.
- Capital programme schemes to deliver new affordable housing including Collyhurst and Silk Street.
- Other elements such as extra care provision in Woodward Court, homelessness.

- Costs to run and deliver the HRA

3.3 In developing the 30-year business plan it is essential that the spending reflects the priorities agreed by members, and there is adequate assurance that the plan is robust and based on sound assumptions. It is essential that the future capital priorities are looked at together with the planned revenue spend.

3.4 The HRA business plan seeks to consider all risks and ensures that any investment decisions are affordable and sustainable both in the short and longer term. It should be noted that whilst the business plan covers 30 years any relatively small changes now can have much larger impacts over the 30 years because of the compounding impact of changes. Therefore, whilst we do look at the business plan over the 30 years, we are primarily focused on the initial 3-year planning period. This is because the assumptions and forecasts are likely to be much more accurate, but ultimately the HRA cannot go into deficit so any indication of potential funding shortfall in the medium term would have to be addressed through savings or cost reductions as part of the budget process in order that the statutory requirement can be adhered to.

3.5 This report is more focused on the revenue elements of the HRA and the budget decisions that will be required for the social housing stock. A fuller report will be brought back to members as part of the budget setting process that sets out the capital investment priorities and the three-year revenue budget position.

3.6 In February 2019, the Government released a policy statement on rents for social housing, which included a direction to the Regulator of Social Housing to have regard for the following when setting the rent standard for registered providers of social housing:

*From 1 April 2020, registered providers may not increase rents by more than CPI (at September of the previous year) plus one percentage point in any year."*

3.7 Due to the current high inflation rates, if the above policy statement was implemented the rents for social housing tenants would be increasing by 11.1% with effect from April 2023, but as part of the Government's Autumn Statement on 17 November, the Chancellor announced that social housing rents will be capped at an increase of no more than 7%. Whilst no decision has yet been made on the rent to be charged, this increase has been reflected in the HRA business plan modelling.

3.8 This report sets out to members the assumptions that are being made as part of the HRA budget preparation. It should be noted that the longer-term budget is based on forecasts and there are many variables that could impact upon the forecasts, in particular the level of future years rent increases.

3.9 HRA reserves are forecast to be around c£90m at the end of the current financial year (2022/23), but they do reduce over the coming years and are forecast to reduce by c£46m by 2026/27 to around £44m. The reductions are mainly due to increased capital investment, and we are forecasting total capital spend of c£137m over the same period and this is mainly funded through the use of reserves. As members will be aware reserves can only be used once, so in order to support further ongoing capital investment over and above the annual budget provision it will require additional borrowing with the associated financing costs that will need to be met through reduced revenue costs or external funding or additional external funding.

3.10 It should be noted that the current plan does not include the majority of works required to enable the Council to achieve its zero carbon targets by 2038, and the costs of retrofitting council stock is estimated to be c.£255m or c£16.5k per property, which will not be achievable from within the ringfenced housing account without government support and/or changes to the current HRA regulations.

## 4. Current Year's Budget Position as at Period 7

4.1 The original approved HRA budget forecast that c£13.188m of reserves would be used in year, this was because of the planned capital investment of c£33m in the current year. As of October 2022, the HRA is forecasting that expenditure will be £17.7m higher than income, and this will be funded through the use of reserves, so in effect the HRA is forecasting an overspend of £4.514m and the main reasons for in year changes are as follows:

- Housing Rents are £0.926m lower than the budget due to a combination of higher numbers of rights to buy in year, which have seen an increase following the pandemic, and a higher than forecast number of void properties. Void properties are higher than the forecast 1%. An improvement plan is in place and is actively reducing the level of void properties, with a corresponding, positive increase in the number of lettings to residents.
- Northwards Housing was brought back into the City Council effective from July 2021, and as part of bringing the service in house to date savings of c£1.6m have been made, and these are due to a combination of reduced accommodation costs, staffing changes and reduced running costs.
- The repairs and maintenance contract is forecast to overspend by £4.2m, this is due to an inflationary uplift of £1.36m and the increased costs of bringing higher number of void properties back into use.
- Heating charges – due to the significant increase in energy costs the cost of gas for tenants' properties is forecast to be c£2.264m higher than budget. Tenants heating charges were increased at the start of the year but have not been increased during the year.
- Private Finance Initiative contractor costs are £0.649m higher than forecast, this is due to a combination of c£400k agreed contract variations and contractual annual inflationary increases above budget of c£249k.
- The above overspends are offset by reduced spend of around £5.756m in respect of Revenue Contribution to Capital Outlay (RCCO). This is

largely due to slippage on several capital investment schemes, including Riverdale maisonettes, installation of ERDF Heat Pumps, and Collyhurst redevelopment. The reasons for this have been separately reported to 14TH September Executive as part of 2022/23 Capital Programme monitoring report.

## 5. Current 2023/24 Budget Assumptions

### Rental Income

5.1 Members may recall that in previous years Government guidance has allowed Local Authorities to increase rents by a maximum of CPI plus 1%. The CPI rate used is based on the September figure in the preceding year, and as at September 2022 CPI was 10.1% and therefore the proposed rental increase would have been up to 11.1% but considering the cost-of-living crisis the Government announced as part of the November spending statement that social housing rents are to be capped at a maximum of 7% for 2023/24.

5.2 The HRA budget is currently being modelled on the basis of a 7% rent increase to all tenants with effect from April 2023 and if this increase is approved by members, it would produce an average weekly rent (based on 52 weeks) of:

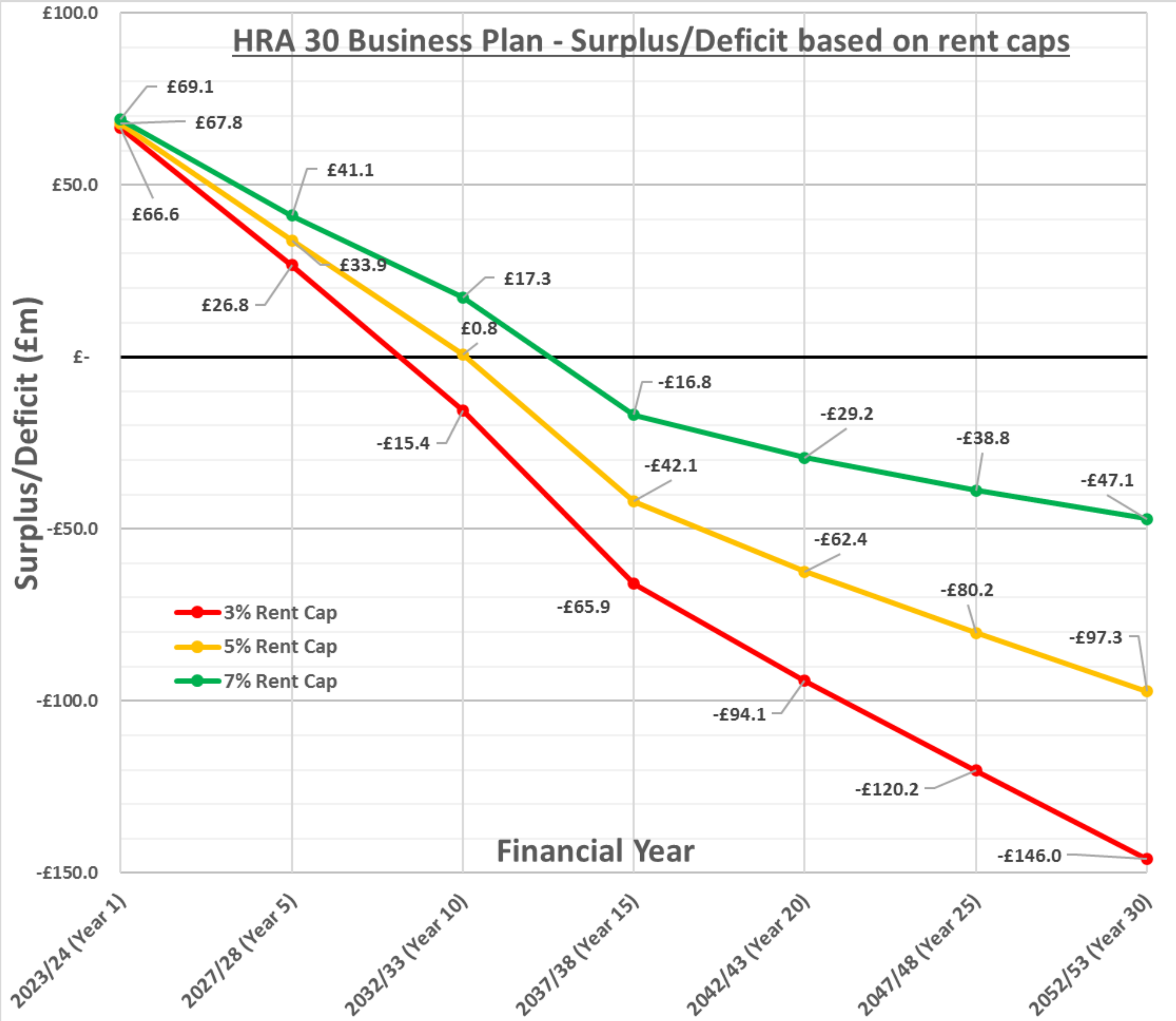
- General Needs £83.88 (£5.49 increase)
- Supported Housing £76.45 (£5.00 increase)
- PFI Managed £98.15 (£6.42 increase)

5.3 Whilst the decision around rent increases has not yet been approved it should be noted that whilst we have used the maximum possible increase of 7% for modelling purposes, the housing benefit levels have not been capped, and if the 7% rent increase is approved by members any increase will be covered in full for those residents in receipt of 100% Housing Benefit entitlement or Universal Credit (housing element) impact of any increase in rents.

5.4 In light of the current economic climate and the potential impact that any rent increase may have on the most vulnerable tenants it is proposed that we continue to budget for a £200k hardship fund to provide targeted support to those most affected by the cost-of-living crisis. The current scheme has already supported 343 households and advanced c£42k to vulnerable residents and it is proposed that the budget for scheme will remain at £200k and be in operation from April 2023 prior to the rent increase coming into effect.

5.5 Whilst the cap on rents is welcomed from a tenant's perspective, there is no cap applied in respect of inflationary impacts on the HRA and a 7% increase results in c£2.5m less rental income in 2023/24 and the impact over the 30-year business plan is an income reduction of c£99m, which could have been used to fund zero carbon works etc.

5.6 The graph below sets out the impact over the life of the business plan of a 7% rent increase, and it also shows the additional impact of lower than 7% rent increases using 3% and 5% for illustrative purposes. At the end of 30 years the deficit with a 7% rent increase is c£47m, but if rents were increased by 3% the deficit increases by around a further £100m.




## 6. Management of Housing Stock and Property Numbers

6.1 The Council continues to own and manage approximately 15,300 properties within the HRA under various arrangements. These include in-house management of c12,400 properties, three PFI schemes that include c2,600 properties, and one management arrangement with Peaks and Plains for 11 properties. There is currently an arrangement with an RP to manage c170 properties in West Gorton, but this contract ends as at March 2023 and it is currently proposed that the management of the stock will transfer to the City Council.

In the 2022/23 financial year Right to Buy Sales (RTB) have increased following the pandemic, and sales of around 240 properties are being forecast in the current year. The number of sales has reduced in recent months and due to the ongoing cost of living crisis and particularly increased interest rates it is forecast that the number of sales will return to drop in the coming years and the budget currently assumes 1.25% for the next five years of the Business Plan, before dropping back to 1% for the remaining years of the plan. This will reduce the level of rent income achieved and the number of sales will continue to be closely monitored. The current business plan does not assume that these assets are replaced within the HRA, and as such the stock is forecast to diminish over time unless a strategy of replacement is adopted, based on current assumptions we will have c11,300 properties at the end of 30 years, if we do not replace any stock.

6.2 At the moment Right to Buy receipts are held separately outside of the HRA and are used to reinvest into affordable housing.

6.3 As referenced at 4.1 above void properties are higher than the 1% forecast as part of the original business plan, and latest figures indicate that there are currently c182 void properties, recognizing the need to get houses back into circulation an officer group has been established in order to review all existing voids and looking to get them back into circulation as quickly as possible. There are currently c100 voids with Equans undergoing works to bring them back into use, and once the backlog of voids is cleared it is anticipated that we will return to normal which is around 520 relets a year. For budgeting purposes, we have assumed that voids will be at around 1% over the coming years.

6.4 Bad Debts – A provision of 1% per annum based on rental income has been built into the business plan, and this is a small increase on the 0.9% forecast for 2022-23. Given the likely pressure that tenants will be under because of the cost-of-living crisis this will need to be kept under review.

***Other Income***

6.5 Other income is forecast to be c.£1.8m in 2023/24 and is assumed that these budgets increase in line with CPI, for 2023/24 we are assuming 8.5% which is a slight reduction on current rates of CPI. The other income budgets are made up as follows:

- Non-Dwelling Rents and Other Income includes:
  - – income from garage rents, rental income from shops and offices, ground rent and telecoms masts - **£296k**
  - Other Income and Contributions – Contributions towards ground maintenance and solar panel income, this includes a one-off receipt of £0.883m in respect of transferring Elizabeth Yarwood Court. - **£1.159m**
- Recharge to Homelessness – rental income in relation to HRA properties used by Homelessness (273 flats/rooms, total income **£233k)**

- Income from Leaseholders (e.g., contribution to heating, cleaning, and repairs to communal areas) - **£112k**

***Private Finance Initiative***

6.6 The PFI schemes are funded through a combination of PFI credits provided by the Government, and rental income for the PFI properties. Whilst we have the option to increase PFI, although they are subject to a capped maximum increase of 7% in line with Government guidance, the Government PFI credits are fixed and do not increase each year and do not reflect any ongoing increases in costs. The PFI contracts are not capped and each of the PFI contracts will increase in line with contractual inflationary increases – for budget purposes the increase is forecast to be 10%.

***Communal Heating***

6.7 In general, it is intended that gas charges are set to reflect the actual cost of gas consumed. However, there are reasons why in practice this is difficult to achieve:

- Charges are set based on anticipated charges for the following year and consumption from the previous year
- Some of the heating systems are not efficient in operation – work is ongoing to improve these.

6.8 Communal heating gas is sourced as part of the City Council overall gas contract and this was renewed in April 2022, at the time of budget setting an increase of c80% was forecast, although due to the global uncertainty in the energy markets the actual increase was 327%. In recognition of the uncertainty in gas prices and to provide some protection to residents the 2022/23 costs for district heating schemes were capped at a maximum increase of 20% in line with the Ofgem cap.

6.9 Gas prices have continued to rise in the current year, and this is reflected in the increased Ofgem cap that was increased by 54% in April 2022 and a further 80% in October 2022. There has been no mid-year review of tenant's energy prices, although tenants will be in receipt of the Government support of monthly payments October – March. Work is ongoing to look at the implications of the huge gas price rises and what heating price rises can be implemented with effect from April to ensure that the HRA is not subsiding tenants heating costs, this may require a longer-term plan in terms of recovering the shortfall over a number of years but details will be brought back as part of the February budget report.

6.10 As part of the Councils Zero Carbon commitment work is continuing to source additional external funding for works, and there continues to be a programme of capital investment that looks to both improve energy efficiency of homes and reduce carbon. This will include c£2m to install new boilers or heat pumps.

*Debt Financing and Borrowing Costs*

6.11 As part of the introduction of self-financing in 2012, there was a one piece of work done by Government to determine what level of debt was affordable, and reallocations of debt were made. As part of the reallocation Manchester received c.£294m as part of reducing the housing debt held at that time, this left a balance of c£121m. The 2023/24 opening HRA debt is anticipated to remain unchanged at £121.26m, and this is funded through a combination of market loans and internal funding using reserves. Using internal funds, provides the benefit of reducing the interest costs of borrowing, but it is important that any future investment decisions are carefully considered because if the reserves fall below the level of internally funded debt, then interest charges will increase. This will be considered as part of any investment proposals that require use of the HRA reserves if the scheme appraisal needs to ensure that the increased costs of borrowing are factored into the project costs.

6.12 Following the removal of Councils' HRA debt caps, which means that there is no upper limit to the absolute level of debt that can be held, the only restriction being that the HRA business plan must demonstrate that any debt can be serviced without the HRA going into deficit.

6.13 The HRA is making provision only for the interest repayments in relation to the outstanding debt. Consideration will need to be given to refinancing the debts as and when the debts become repayable this will be considered as part of the treasury management strategy.

*Operational Housing - Stock Management Fee*

6.14 The decision to bring Northwards housing back into the Council was approved by the Executive in September 2020, and it was one of three options considered and part of the decision was based on the business case forecasting annual savings of £2.4m. To date annual savings of c£1.6m have been achieved and this is through a combination of staff savings and savings in accommodation costs following the cessation of the lease at Hexagon Tower.

6.15 Work is still ongoing to review the existing delivery models, and is expected to lead to further savings being identified, but these the value or timeline of any savings have not yet been determined there are no savings built into the business plan, although this will be updated once known The 2023/24 costs of operational housing are forecast to be c£14.7m, this is an increase of £0.528m on the current years budgets, and this reflects the impact of the 2022/23 pay award and a 4% provision for 2023/24 pay awards.

*Repairs and Maintenance Contract*

6.16 The repairs and maintenance contract was let to Equans with effect from March 2021 and 2021/22 was the first year of operation. The indicative contract budget for 2022/23 is c£15m.

6.17 Upon the first anniversary of the contract the budget should have been uplifted in line with BCIS inflation which at that point would have meant a contract uplift of c14.1%. It was agreed to move to a cost plus contract linked to CPI +1% (9.9%), although actual costs charged are based on the actual costs incurred plus an overhead. At year end any costs over or under the budgets are subjected to the pain/gain mechanism whereby the impact of any under/overspend is shared on a contractually agreed basis between Equans and MCC. The 2022/23 has seen significant cost increases linked to inflation and the higher volume of work being delivered.

***Inflation Assumptions***

6.18 The HRA budget includes inflation assumptions in line with the Council's current assumptions in relation to pay and prices. Most of the inflation in the business plan is linked to the consumer price index rate (CPI), which have increased sharply lately. Based on an assessment of forecasts available, CPI has been forecast to peak at around c.8.5% in 23/24, and then fall back to c5.25% in the in 2024/25 the business plan assumes 2.75% in 2025/26 before reducing back to a 2% CPI rate for the remainder of the plan.

***Garage Rents***

6.19 Unlike housing rents there is no cap on the garage rents, and it is proposed that 2023/24 garage rents are increased in line with the original rent formula, so if approved by members garage rents will increase by 11.1%, and the impact of the increase is shown in the table below:

| | Annual Charge 2022/23 | Weekly Charge 2022/23 | Proposed Weekly Charge 2023/24 | Proposed Weekly Increase |
|---|---|---|---|---|
| **Site Only** | £107.12 | £2.06 | £2.29 | £0.23 |
| **Prefabricated** | £237.64 | £4.57 | £5.07 | £0.50 |
| **Brick Built** | £279.24 | £5.37 | £5.97 | £0.60 |

## 7. Reserves Forecast

7.1 Based on the latest budget position we are forecasting that the reserves position as at the end of March 2023 will be c£90.1m and this reduces by c£46m over the next three financial years to around c.£44m, this is mainly to do with the planned capital investment over this period. Current projections show that the reserves do go into negative around 2035/36 and are forecast to be around £47m at the end of the 30 years. Given this cannot happen work is required to identify means of either reducing HRA costs or generating additional income in order to ensure that the HRA is sustainable throughout the life of the business plan. It should be highlighted that the significant costs of undertaking all the required carbon retrofitting works are not yet included in the business plan. The costs of this work are estimated to be around c£16.5k per property, and this will inevitably require additional external resources in order to ensure all works can be undertaken.

## 8. Conclusions

8.1 This report provides members with an update on the work being undertaken to develop the 2023/24 HRA budget, it recognizes the difficulties faced by tenants in light of the current cost of living crisis whilst seeking to balance the need to have a balanced HRA business plan.

8.2 The budget proposals will allow for continued service delivery and investment within the existing stock and development of new HRA stock within the confines of the available resources, although there are pressures around meeting the ambition of the climate agenda.

## 9. Key Polices and Considerations

### (a) Equal Opportunities

The rents have been set in line with the Government's guideline rent.

### (b) Risk Management

Under the provisions of the Local Government and Housing Act 1989, the Authority must ensure that the Housing Revenue Account does not result in a debit balance. The proposed change in rents and identification of savings within this report, together with regular budget monitoring will assist in managing this risk over the short term. Work will continue to ensure that the HRA remains viable in the longer term.

### (c) Legal Considerations

The City Solicitor has reviewed this report and is satisfied that any legal considerations have been incorporated within the body of the report.