Report Number: SWT 118/21

Somerset West and Taunton Council

Executive – 15 December 2021

Draft 2022/23 Housing Revenue Account Budget Update

This matter is the responsibility of Executive Councillor Smith, Housing

Report Author: Kerry Prisco, Management Accountant & Reporting Lead

1 Executive Summary

1.1 The purpose of this report is to provide Members with an update on progress of the Housing Revenue Account (HRA) regarding Budget Setting for 2022/23, the latest Medium Term Financial Plan (MTFP) forecasts, the 30-Year Business Plan, and the areas to be finalised.

1.2 The HRA's initial MTFP (Feb 2021) projected an early indication of a budget Gap of £328k. Since then the economic operating environment has become significantly challenging compounding the financial position.

1.3 The Housing sector is currently seeing the most challenging period in a generation, in terms of the multiple crystallisations of risks and competing demands on the service both operationally and financially.

1.4 A review of baseline budgets and up to date information has identified further growth and savings for inclusion within the MTFP. This has led to the HRA's current MTFP projection of a budget gap for 2022/23 of £1.696m. Plans to mitigate this additional financial pressure will be included in the Draft Budget report to Members in the new year.

1.5 It is anticipated that 2022/23 will be the final budget year for Somerset West and Taunton as a district Council with its assets, liabilities, and functions due to transfer to the new Somerset unitary council once it is created. Further work is required to understand what the budget gap for the HRA might be from 2023/24 onwards.

1.6 The budget planning process is ongoing and there remains some areas where estimates are to be finalised therefore the estimated Gap is likely to change and will be reflected in the final draft Budget. The Executive is due to recommend its final budget proposals to Full Council in February 2022.

2 Recommendations

2.1 This report is to be noted as the latest Medium Term Financial Plan forecasts and action required to finalise the 2022/23 Budget.

3 Risk Assessment

3.1 It is evident that financial pressures within the Housing service present a significant risk to affordability of existing plans in the short term. Measures will need to be implemented to ensure 2022/23 budget is balanced and adequate minimum reserves are maintained.

3.2 There remain some specific key risks within the budget and medium term forecasts that will be managed by officers and/or portfolio holder. These are summarised in section 8 of the report.

4 Background and Full details of the Report

4.1 The Housing Revenue Account (HRA) is a ring-fenced, self-financing account where income from tenants and sale of assets funds the homes and related services provided to tenants, and investment in the provision and quality of council owned housing stock.

4.2 The Council has a long-term business planning approach to managing the stock and the finances within the HRA, which is reported separately. The financial strategy for the HRA focusses on ensuring that spending and capital investment plans are affordable and contained within the projected resources available.

4.3 The Budget Setting Report for 2021/22, presented to Full Council in February 2021 provided a balanced budget, the latest MTFP forecast and an update on the 30-Year Business Plan. Independent financial planning advice was commissioned from Altair to support the business in undertaking this in-depth review; to provide challenge to our existing assumptions, to consider the financial impact of the COVID pandemic and provide assurance in the HRA's ability to deliver the new build aspirations.

4.4 The outcome of this review highlighted minimal general reserve balances in 2022/23 (see Table 1) along with reduced interest cover (see Table 2), however the forecast showed that the HRA met and improved upon this over the 30-year period. This did however highlight that in the short to medium term we are operating close to business plan limits in terms of adequacy of reserves and affordability of capital investment plans. The Business Plan contains limited flexibility in the short term. This was considered an acceptable level of risk at the time to deliver the proposed capital programme comprising both maintaining existing stock and allowing for the new build / purchase of additional stock.

Table 1: HRA General Reserve Balances as at 2020/21 Projections

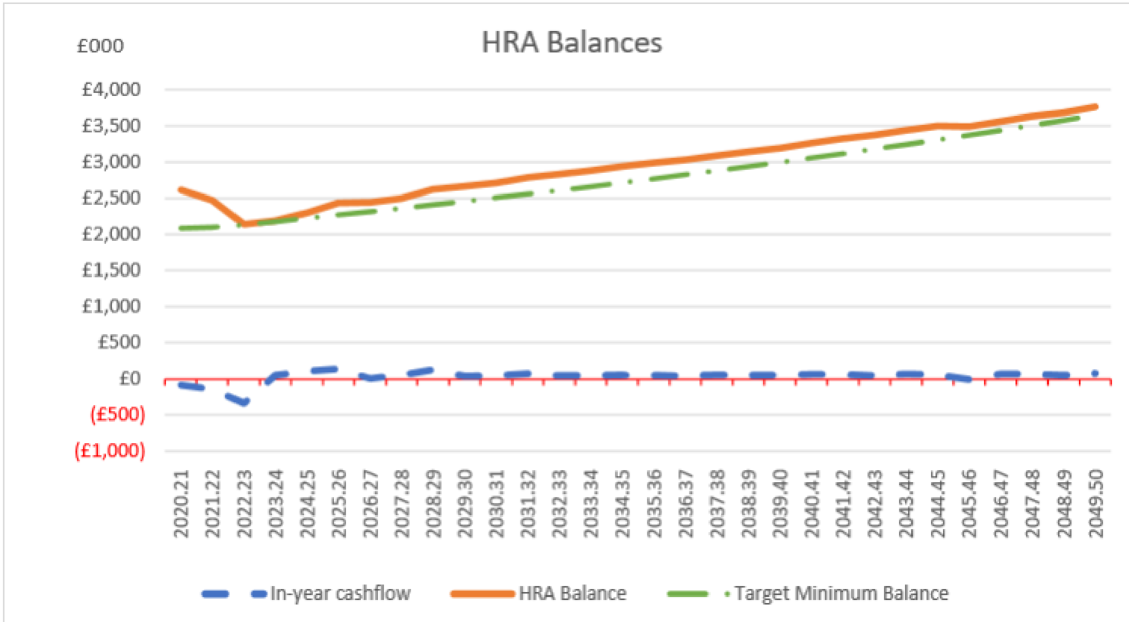
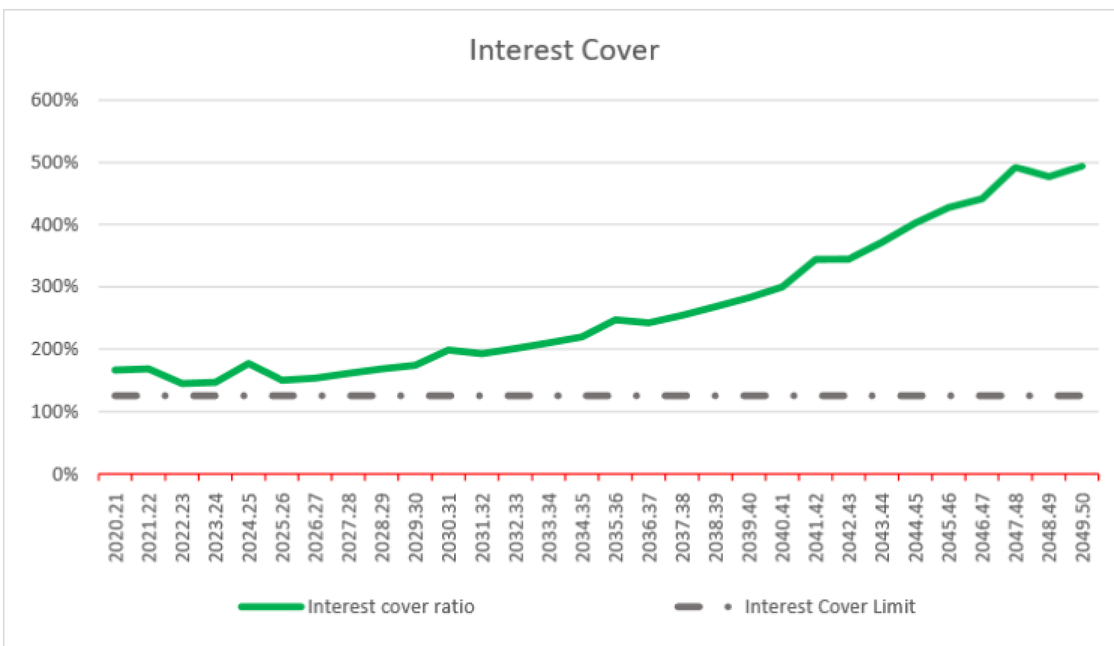


Table 2: HRA Interest Cover as at 2020/21 Projections



4.5 The MTFP forecast presented at that time also predicted a budget gap of £328k in 2022/23, with an improved position in later years. There was capacity at the time to under write this with one-off funding from reserves whilst officers worked to find sustainable options to close the Gap.

Table 3: HRA Revenue Budget for 2021/22 and Medium Term Financial Plan

	2020.21	2021.22	2022.23	2023.24	2024.25	2025.26
	£000	£000	£000	£000	£000	£000
Income						
Dwelling Rents	- 24,225	- 24,951	- 25,682	- 26,533	- 28,315	- 28,712
Non Dwelling Rents	- 719	- 704	- 713	- 724	- 737	- 748
Service Charges	- 1,457	- 1,623	- 1,661	- 1,702	- 1,750	- 1,794
Other Income	- 371	- 389	- 396	- 404	- 413	- 422
Total Income	**- 26,773**	**- 27,668**	**- 28,452**	**- 29,364**	**- 31,215**	**- 31,676**
Expenditure						
Repairs and Maintenance	5,901	6,795	6,917	7,055	7,218	7,387
Supervision and Management	3,905	3,731	3,817	3,912	4,022	4,122
Rents, Rates, Taxes and Other Charges	311	305	311	317	324	331
Special Services	1,058	1,058	1,083	1,110	1,141	1,169
Bad Debt Provision	180	180	180	180	180	180
Contribution to CDC	229	229	233	238	243	248
Transfer to GF	3,622	3,216	3,274	3,340	3,416	3,485
Total Expenditure	**15,206**	**15,515**	**15,815**	**16,152**	**16,544**	**16,922**
Other Expenditure						
Depreciation - dwellings	6,511	7,342	7,474	7,624	7,799	7,955
Depreciation - non dwellings	490	321	327	333	341	348
Interest Payable	2,745	2,669	3,343	3,580	3,690	4,294
Investment Income	-	-	-	-	-	-
Provision for Repayment of Debt	1,821	1,821	1,821	1,624	2,733	2,018
Revenue Contribution to Capital	-	-	-	-	-	-
Movement in Reserves						
Total Other	**11,566**	**12,153**	**12,965**	**13,161**	**14,564**	**14,615**
Total - (surplus) / deficit	**-**	**-**	**328**	**- 51**	**- 107**	**- 138**

4.6 Since the Budget Setting 2021/22 report was produced the economic operating environment has become significantly challenging compounding the financial position.

4.7 The Housing sector is currently seeing the most challenging period in a generation, in terms of the multiple crystallisations of risks and competing demands on the service both operationally and financially. Examples of headline key issues that are having a financial impact are as follows:

4.7.1 Brexit and the COVID pandemic has created further contractor uncertainty and labour market shortages. Labour and materials are costing on average significantly more and additional costs such as insurances have seen uplifts in the market.

4.7.2 Staff recruitment and retention, shortages of key skills and trades with significant salary inflation, meaning the Council is facing pressure to be competitive in the recruitment market, this is compounded by uncertainty about the future due to organisational change.

4.7.3 Covid-impact on the demands on the service from complex case work and community vulnerability.

4.7.4 Covid-locally, due to taking appropriate public health precautions during the covid pandemic we still have backlogs in both repairs and capital works the team are working hard to address.

4.7.5 Supply chain challenges and current economic position driving up costs.

4.7.6 Customer demands continue to increase for the sector in terms of expectations on what social landlords can provide and how they go about service provision, with complaints increasing across the sector.

4.7.7 Regulatory impacts post the Grenfell tragedy are continuing to increase with the current and future requirements of the Regulator and the Housing Ombudsman increasing pressures on the service.

4.7.8 Staff wage bill pressures with potential pay increases, pension pressures and additional National Insurance contributions.

4.7.9 Net Zero carbon and retrofit, more work is to be done to plan for and model the financial and operational impacts of retrofit of our properties with early projects proposed for next year.

4.7.10 Regeneration impact, we have a period of reduced stock numbers whilst new properties are constructed at North Taunton, with the reduction in income impacting us at the current time.

4.8 This has therefore placed the HRA revenue account under significant financial pressure and can be seen in the Quarter 2 Financial Monitoring Report, being presented to Members through the same committee cycle. This has also further exacerbated the budget gap predicted for 2022/23.

4.9 The changes to the base budget identified to date are reflected in the updated MTFP figures below in Table 4. The Gap has increased significantly, and Officers are still reviewing the detailed budget estimates to ensure that a balanced budget is presented to Full Council in February 2022. There are still some items which are unknown at this stage of the budget process which are summarised in Section 7.

Table 4: Summary 2022/23 Budget Gap Reconciliation

	£k	£k
2021/22 Balanced Budget		0
Service Cost Pressures:		
Net of Interest Payable / Receivable	131	
Net of Staff Growth / Savings	157	
21/22 Proposed Pay Award of 1.75%	116	
22/23 Proposed Pay Award of 2%	137	
National Insurance of 1.5%	48	
Shared Support Staff charged to the HRA	33	
Pension Deficit charged to the HRA	16	

	£k	£k
Repairs & Maintenance Material and Contract Cost	1,585	
Grounds Maintenance	33	
Insurance	24	
Sewerage	44	
Compliance	67	
CCTV Contract	7	
Waste Disposal	10	
Fleet Contract and Fuel	97	
Radon	88	
Policy & Management	87	
Business Rates	37	
Health & Safety	59	
Street Lighting	17	
Other	3	
Subtotal – Service Cost Pressures		**2,796**

Service Cost Savings:		
Dwelling Rental Income (assuming implementation of crrent rent policy)	630	
Non-Dwelling Rental Income	63	
Income for Services / Facilities	25	
Other Income	19	
Supply Chain Procurement Savings	50	
Tenancy Management	28	
Capitalisation of Development Staff Time	285	
Subtotal – Service Cost Savings		**1,100**
2022/23 Latest Budget Gap Estimate November 2021		**1,696**

5 Closing the Gap

5.1 The Gap has increased significantly, and it is important that the leadership team focusses on delivering sustainable options to control spending. It is vital that costs are managed within annual income totals to ensure ongoing affordability of services. This may require pulling back operations to focus on delivering essential and statutory functions as a minimum to counter the gap increase.

5.2 The budget setting process this year will be very challenging with some difficult decisions to make on how we generate sufficient savings in both the short and medium term, that we have not encountered for some time for the HRA. Solutions will inevitably lead to an impact on service delivery and discretionary activities but we will also look for treasury solutions within the business plan to assist us.

5.3 The leadership team and the Executive will develop plans to close the additional gap and share this for consultation with members through the budget setting process.

6 HRA Reserves

HRA Unearmarked Reserves

6.1 The current recommended Minimum Reserve Balance is £2m. The S151 Officer will review the minimum reserve requirement in February 2022 as part of the final budget recommendations.

6.2 The HRA unearmarked reserves are currently estimated to be at £2.492m at 31 March 2022 as per Table 5 below. This is £492k above the recommended minimum balance of £2m. This position is reliant upon the current year outturn position being maintained or reduced. If reserves fall below adequate minimum levels, then plans will need to be put in place to restore these to acceptable levels to maintain financial resilience in future years.

Table 5: HRA Unearmarked Reserve Balance

	Approval	£'000
Balance Brought Forward 1 April 2021		**2,686**
Approved - OC & Supply Chain Project Lead	Director / S151	-19
Approved - Housing Policy Lead x1	SMT	-40
Approved - Housing Performance CM (Complaints) x1	SMT	-25
Approved - Housing Improvement Programme Manager	SMT	-80
Approved - Compliance Administrator	SMT	-23
Approved - Stock Condition Surveyors x2	SMT	-89
Approved - Landlord Compliance Specialist	SMT	-33
Approved - Building Safety CM	SMT	-25
Approved - Assets Admin Assistant	SMT	-18
Approved - Electrical Supervisor	SMT	-28
Approved - Tradesperson	SMT	-21
Approved - Released EMRs	Full Council – 05.10.21	869
Approved - 1.75% Pay Award	Executive – 15.09.21	-175
Provisional - Share of Additional H&S Costs	Director	-96
Provisional – Release further EMRs	Executive	175
Forecast Balance after current commitments		**3,058**
Projected Outturn - Total variance		-566
Forecast Balance 31 March 2022		**2,492**
Recommended Minimum Balance		2,000
Projected Balance below recommended Minimum Balance		492

6.3 The S151 Officer advises that it is prudent to retain headroom within the general reserves balance to provide financial resilience. Financial pressures this year have demonstrated the potential scale of financial risks. These will almost certainly be exacerbated with the anticipated requirement to contribute towards the implementation costs of the new unitary authority and in an increasingly volatile operating environment.

HRA Earmarked Reserves

6.4 The HRA Earmarked Reserves are currently estimated to be nil at the 31 March 2022. These are at the lowest level seen and do not provide any additional financial resilience for the business.

Table 6: HRA Earmarked Reserve Balance

Description	Balance B/F £000	Return to General Reserves	Use in 2021/22	Balance C/F £000
HRA One Teams	26	-20	6	0
HRA Social Housing Development Fund	849	-849	0	0
HRA Hinkley	57	0	57	0
HRA Contribution to Change	175	-175	0	0
HRA Total	**1,107**	**-1,044**	**63**	**0**

7 Areas Still to be Completed

7.1 Budget Holders will put forward their proposals for Fees and Charges and the impact of these will be reviewed by Finance. The S151 Officer has delegated authority to agree these and an update will be provided within the next budget update report.

7.2 Further information that relate to the level of income projected and / or savings being offered are still being reviewed.

7.3 The projections on the capital programme for 2021/22 and 2022/23 still need to be finalised and reviewed for affordability. There is some flex in the programme that could have an impact on the overall position of the HRA in terms of borrowing and investment of surplus balances.

7.4 IFRS 16 (Finance Leases) comes into force from 2022/23 which changes the way we account for leases. The council also has a new corporate fleet contract that commenced in October. Both elements of this are currently being worked through to reflect the revenue and capital budget requirements.

8 Risk, Opportunities and Uncertainty

8.1 Ongoing risks and uncertainty for the budget at this stage include:

8.2 **Dwelling Rent and Service Charge Income:** Linked to (a) regulator changing legislation to force a rent freeze or rent reduction, (b) CPI rates, (c) political pressures to reduce rents. The HRA Business Plan and our ambitions rely on the assumption that our rent policy of CPI +1% will continue, however if this were to be reduced then it would create additional budget pressure.

8.3 **Repairs & Maintenance:** Overall this is a very demand led and reactive service based on the needs of the tenants. There are also a number of uncontrollable variables associated with this service such as the weather (e.g. cold winters causing burst pipes, roof leaks, etc), condition of properties when returned (e.g. void refurbishments), consumer demand on minor internal / external repairs (e.g. broken door or fence) and the type of repair work required. As such the levels of demand do not always follow a recognisable trend. We therefore have to caveat the forecasts in these areas to account for fluctuations. The economic operating environment has also been compounded, namely by Covid and Brexit, creating contractor uncertainty and labour market shortages and inflating the cost of materials and labour.

8.4 **Trade Salaries**: We are experiencing a significant increase in construction related salary costs in the sector, with shortages of some key trades for example electricians. This can mean that some of our salaries are no longer competitive in the market. We have conducted a review of some of our salaries and will be making some changes here, and the cost of this change is incorporated into our MTFP, however as this review process progresses across all trade areas it may create further revenue pressures that need to be addressed.

8.5 **Pay Award**: The budgets have been set based on 1.75% pay award for 2021/22 and then 2% for 2022/23. The annual pay award negotiations are still taking place.

8.6 **COVID-19:** The ongoing impact of the pandemic presents a risk to the Housing Service, particularly in terms of revenue collection as well as impact on tenant mental health and wellbeing. We have already seen an increase in inflation rates impacting our future income and expenditure, however another significant risk relates to financial hardship that could result from the impact of COVID, following the ending of government support such as furlough and the uplift in Universal Credit. If the net result is higher unemployment and much tighter finances for many households, this could impact on their ability to pay rent. Furthermore, there may be an increasing demand and therefore budget implication for support services for tenant households affected by the impact of COVID. This could present across a range of service demands including increased debt and benefits advice;

unemployment support, mental health support; anti-social behaviour intervention, safeguarding and domestic abuse support.

8.7 **Unitary Authority:** The Secretary of State has announced his decision on the future of local government in Somerset and has chosen the One Somerset option put forward by the County Council. This means there will be one new council for Somerset replacing the existing five councils. There is a structured timetable to follow for implementing the change so the new council can come into effect on 1 April 2023.

8.8 It is currently unknown what the future potential costs will be as a result of this decision, and what the HRA's share will be, and whether these costs will need to be funded using revenue or capital budgets. From a capital perspective the business plan does provide some headroom to allow non-right to buy (RTB) receipts to be used as flexible capital receipts to fund transformation costs. However this direction ends on the 31 March 2022 and it is unknown if the government will approve an extension on this directive, although they have recently signalled this intent. If the costs can only be treated as revenue then we may need to review other expenditure to make this affordable and or consider the use of reserves.

8.9 **Right To Buy (RTB) Receipts:** This is a government scheme that enables tenants to purchase their homes at a discount, subject to meeting qualifying criteria. The receipts allowed to be retained by the Council can now fund up to 40% of new social housing costs and must be used within five years of receipt, following an amendment to the scheme policy from the 1 April 2021. To date, the Council has successfully spent all of their retained 1-4-1 receipts resulting in no returns being made to the Treasury/MHCLG.

8.10 **Welfare Reform and Universal Credit:** The impacts of Welfare Reform and Universal Credit remain a risk, with the number and value of rent arrears still under upward pressure as more tenants switch to universal credit. Mitigations are already in place to help support tenants affected by Welfare Reform and Universal Credit such as debt advice, access to discretionary housing payments and an arrears management team with redesigned workflow processes.

8.11 **Decent Homes Standard:** Changes to the Regulator of Social Housing's decent home standard as well as higher thermal efficiency standards which are unsupported by additional external grant funding would place an additional burden on HRA resources available for elemental investment in homes. Once the detail is known, we will need to adapt to ensure we continue to maintain stock at the Decent Homes Standard and prepare to meet all the evolving expectations, incorporating the financial impacts into the Business Plan.

8.12 **Building Regulation and Fire Safety:** The Grenfell Tower fire and subsequent Review of Building Regulation and Fire Safety bring a number of operational and financial risks. These risk have been mitigated with the increases in revenue and capital budgets proposed for 2021/22 for compliance related work. However the exact costs are currently unclear. There are likely to be other impacts as a result, such as impacts on the repairs budget due to additional work to communal areas, more intensive management of flat blocks and further resilience within teams to respond to the volume and breath of enquiries. We will need ensure continued compliance with these statutory requirements.

8.13 **Housing White Paper:** In November 2020 the Government published the Housing White Paper which sets out the changes to how social landlords will operate. It will require a number of changes to home safety, tenant satisfaction measures, complaints handling, a new inspection regime for social landlords and a strengthened role for the Regulator of Social Housing. Many of the new changes in the white paper have already been mitigated in Housing by strengthening our compliance activities, setting up the new Housing Performance Team to be responsible for communications, performance data and engagement but this will need to be kept under review and self-assessment has begun.

8.14 **Retrofit by 2030:** There is a duty for social landlords to improve the energy efficiency of its homes. The national climate change requirements set by government under the Clean Growth Strategy 2017 requires all social landlords to achieve EPC C by 2035. However the strategy also requires landlords to achieve EPC C by 2030 where tenants are in fuel poverty. Therefore it is prudent to achieve EPC C by 2030.

8.15 **New Build Homes and Phosphates:** The HRA has a significant pipeline of new homes to be delivered over the next 8 years. Some of these homes require phosphates mitigation strategies to gain planning approval. There remains uncertainty on the ability of the council to mitigate for phosphates. This may result in less affordable housing development and less capital spend.

9 2022/23 HRA Capital Programme

9.1 The current HRA approved Capital Programme is £118.3m. This consists of £100m for the Social Housing Development Programme, which will be delivered over the next 8 years, and £18.3m for the Majors & Improvement Programme to be delivered in 2021/22. The current year performance against this approved budget can be found in the quarterly financial monitoring report.

9.2 Officers are currently reviewing the draft capital programme for 2022/23 to ensure that this is focused on service priorities for the forthcoming year, that the business has the capacity to deliver the programme operationally and that the programme is affordable in terms of financing available so that this does not impact negatively on the revenue budget gap. The final proposal will be included in the next report to Members.

10 Links to Corporate Strategy

10.1 The Council's MTFP underpins the planning of resources needed to meet the priorities and objectives within the Corporate Strategy and related plans.

11 Finance / Resource Implications

11.1 The Council's financial position is set out above within the body of this report.

11.2 It is important that Councillors have a good understanding of the financial position and forecasts over the medium term.

12 Legal Implications

12.1 The Council is required by law to set a balanced budget and failure to do so would result in serious financial and service implications and lead to Government intervention.

13 Climate and Sustainability Implications

13.1 There are no direct carbon/environmental impacts arising from the recommendations. Budgeted support towards the Council's climate and sustainability priorities is included within the MTFP.

14 Equality and Diversity Implications

14.1 There are no direct equality or diversity impacts arising from the recommendations within this report. Officers and members will need to consider whether there are any impacts for detailed policy updates and proposals within the detailed budget plans as these are developed and presented for decision.

15 Partnership Implications

15.1 The Council's HRA budget includes expenditure on services provided by other key partners such as MIND, citizen's advice, Inspire to Achieve, Taunton East Development Trust, North Taunton and Wiveliscombe Area Partnership.

16 Asset Management Implications

16.1 Clearly the revenue and capital budgets for the HRA include provision for maintaining our housing stock in accordance with relevant standards. The Housing Asset Management strategy also encourages proactive treatment of poorly performing stock from both a financial and social perspective which will be important considerations for the future efficient operation of the service.

17 Scrutiny Comments / Recommendations

17.1 This report was considered, and the recommendations supported by the Community Scrutiny Committee on 24 November 2021.

17.2 The main comments and questions were related to:

17.2.1 The repairs and maintenance, staffing and radon growth items. The Director of Housing provided explanation of key posts required to deliver operational activity in the year new and the one-off budget required to survey a number of properties for radon.

Democratic Path:

- **Community Scrutiny – 24 November 2021**
- **Executive – 15 December 2021**
- **Full Council – No**

Reporting Frequency: Ad -hoc

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