Housing, Homelessness and Fair Work Committee

10.00am, Thursday, 18 March 2021

Housing Revenue Account (HRA): Impact of a one-year rent freeze

Executive/routine	**Executive**
Wards	**All**
Council Commitments	

1. Recommendations

1.1 It is recommended that Housing, Homelessness and Fair Work Committee:

1.1.1 Notes the impact of this one-year rent freeze on the 2021/22 revenue budget; and

1.1.2 Agrees that the mitigations to the one-year rent freeze will form part of the annual HRA Business Plan review and 2022/23 budget consultation process.

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Report

Housing Revenue Account (HRA): Impact of a one-year rent freeze

2. Executive Summary

2.1 On 18 February 2021, the City of Edinburgh Council approved a composite motion from the Conservative, Green and Liberal democrat groups. This motion agreed '*the recommendations by the Executive Director of Place in the Housing Revenue Account Budget Strategy for 2021/31 and the outline 10-year HRA capital programme 2021-31, subject to agreement that there be no rent rise in 2021/22; implementation of the amendments…and any revisions needed to the capital programme as a result.*'

2.2 It also agreed the acceleration of £1.86m of capital investment to deliver improvements to internal common stairwells through a prioritised programme of refurbishment across 180 blocks. As well as, additional resource of two surveyors and one case officer for the Mixed Tenure Improvement Service (MTIS) to accelerate property surveys and work with owners to bring forward works to the value of £4m.'

2.3 The reduction in rental income and acceleration of mixed tenure improvement is to be funded through contingency funding and reserves from 2021/22; with the position being subject to annual review of the budget strategy.

2.4 This report sets out the impact of this one year rent freeze on the 2021/22 revenue budget, and the potential mitigations that need to be put in place in 2022/23 to secure the 10-year £2.8bn capital investment programme to deliver Council commitments, including the delivery of new homes, net zero carbon emissions by 2030, to create places where people want to live that keep them safe, secure, healthy and connected through a holistic area-based regeneration approach.

3. Background

3.1 On 5 November 2020, Housing, Homelessness and Fair Work Committee considered a report on the HRA Budget Strategy 2021/22, which set out the initial findings of consultation with tenants, a significant increase in capital investment over the next ten years to support the delivery of new affordable homes, achieve net zero carbon and improve existing homes and neighbourhoods where Council tenants live. It also provided a progress update on the delivery of service improvements.

3.2 On 2 February 2021, Finance and Resources Committee approved the 2021-2031 HRA budget Strategy which included a plan to invest £2.8bn over ten years to deliver Council commitments, including the delivery of new homes, net zero carbon emissions by 2030, funded by a 2% rent increase. The report was referred onto the City of Edinburgh Council for approval.

3.3 On 18 February 2021, the City of Edinburgh Council approved a composite motion from the Conservative, Green and Liberal democrats. This motion agreed '*the recommendations by the Executive Director of Place in the Housing Revenue Account Budget Strategy for 2021/31 and the outline 10-year HRA capital programme 2021-31, subject to agreement that there be no rent rise in 2021/22; implementation of the amendments set out in paragraphs 4-6; and any revisions needed to the capital programme as a result.*'

3.4 The full composite motion is as follows:

3.4.1 Notes that over the last year there has been a delay in capital programmes and a reduction in repairs and maintenance activity in council housing.

3.4.2 Notes that council rents in Edinburgh are the highest in Scotland by some way, 30% above the Scottish average; and that, notwithstanding the availability of housing benefit and universal credit to cover rent rises for half of tenants, for those at the margin, a rent rise of £100 a year on low and fragile incomes is significant.

3.4.3 Agrees that, in view of the ongoing negative impact of the pandemic and the economic recession, to agree to freeze council house rents for one year only.

3.4.4 Welcomes the necessary investment in external fabric and communal areas of blocks where the Council is a majority owner within the draft HRA five-year Capital Investment Programme.

3.4.5 Agrees acceleration of £1.86m of investment to deliver improvements to internal common stairwells through a prioritised programme of refurbishment across 180 blocks.

3.4.6 Approves additional resource of 2 surveyors and 1 case officer for the Mixed Tenure Improvement Service (MTIS) to accelerate property surveys and work with owners to bring forward works to the value of £4m.

3.4.7 Agrees to manage this exceptional rent freeze and essential accelerated fabric investment through contingency funding and reserves during 2021/22 with the position being subject to annual review of the budget *strategy with updated assessments of delivery of the Capital Investment Programme and Investment Strategy to be considered.*

4. Main report

4.1 The HRA is funded from tenants' rents, fees and service charges for services provided to tenants and assets held on the HRA account. The HRA is self-contained and has no direct impact on the Council's General Fund budget.

4.2 The 2021-2031 HRA budget Strategy, presented to Council on 18 February 2021 included a plan to invest £2.8bn over ten years to deliver Council commitments, including the delivery of new homes, net zero carbon emissions by 2030, funded by an annual 2% rent increase. This is an ambitious strategy sought to significantly increase the number of new council homes, whilst doubling the average investment in existing homes and regenerating wider estates. The strategy was funded by driving forward management efficiencies, robust debt management and a stable, often below inflationary, 2% rent strategy.

4.3 Over the last five years the majority (over 80%) of tenants who responded to previous budget consultations told us that they supported the investment plan, funded by a 2% rent increase, identifying the following priorities to be delivered:

4.3.1 building new affordable homes;

4.3.2 investing in making existing homes easier and cheaper to heat;

4.3.3 improving core housing services, such as day to day housing management, and repairs and maintenance of Council homes, as well as wider estate management; and

4.3.4 reducing the cost of living through the delivery of a variety of different services, including, for example, an energy advice service, a tenant discount scheme, and community food growing.

4.4 This year's consultation also sought tenants' views on the changing focus of the investment strategy from investing in the interiors of homes, to buildings and neighbourhoods. It generated a similar profile of responses, with 76% of tenants confirming support for the investment plan funded by a 2% rent increase, with a further 22% supporting increasing rents beyond 2%, if priorities could be delivered more quickly.

4.5 The composite motion approved by Council on 18 February sought a one-year rent freeze, whilst maintain the delivery the £2.8bn capital investment programme, alongside an acceleration of £1.86million into 2021/22 to deliver common stair improvements (including upgrades to windows, walls, ceilings, balustrades and handrails, stair painting, and improved lighting) and an additional revenue resource for the MTIS service. Council approved the additional resource of two surveyors and one case officer for MTIS accelerate property surveys and work with owners to progress works in mixed tenure blocks. An additional £0.167m has been included in the revised 2021/22 HRA budget set out in Appendix 1. The additional staff are expected to generate c.£4.0m in capital works. The 20% project management fees (c.£0.800m) will ensure that the MTIS is self-financing and the HRA is reimbursed. The detailed HRA Capital Programme 2021/22 report also being considered by committee includes the acceleration of common stair improvements and the HRA contribution to the additional capital works generated by the expansion of the MTIS team.

4.6 Throughout the pandemic the Housing Service has continued to provide housing management, estate management, essential repairs and maintenance service. No staff have been furloughed, so substantial fixed costs remain. The Place Directorate Revenue Monitoring 2020/21 - month nine report, also being consider at this committee, projects a balanced position for the HRA in 2020/21 financial year after providing £10.598m from revenue for planned capital investment programme in forthcoming years. However, this forecast is dependent on additional costs as a result of COVID-19 on operations. Significant adjustments have been made to services to comply with government guidance and protect tenants and staff, including adjustments to buildings to manage social distancing, staff training, equipment and materials, staff shielding and absence due to ill health, allowances for extra time for cleaning, repairs and maintenance and facilitating social distancing. The month nine forecast has estimated operational costs for COVID-19 related measures to be £3.316m by year end.

4.7 A one-year rent freeze means a reduction of £2.014m in projected gross rental income in 2021/22, or £1.939m in net income. Unless income is increased in future years to compensate this equates to a £93.921m reduction over the lifetime of the business plan. It also increases the overall deficit by 179% from £25.300m to £70.594m, lasting two years longer (2029/30 – 2043/44).

4.8 The proposed budget (funded by a 2% rent increase), projected an average annual deficit of £1.9m over these 13 years. However, it is important to note that the deficit only related to in-year expenditure exceeding income and there was enough in reserves to completely offset it. Whilst there is enough in reserves in 2021/22 to cover this loss income, the reduction of c.£2m revenue income year after year means that there will be less reserves and contingency built up prior to the deficit years and greater in-year deficits to be offset during the deficit period. Once reserves are exhausted, the contingency would be called on to seek to balance the budget. The combined effect of the rent freeze means the reserves and ringfenced contingency are exhausted by year 13 (five years into the deficit period), only recovering in year 30 of the plan.

4.9 In order to mitigate the impact of a one-year rent freeze longer term and return the Business Plan to a healthy financial position, there are four potential options:

4.9.1 **Increase income in future years –** in order to minimise the impact on the Capital investment Programme rents would need to be increased by a minimum 2.5% over the next four years. If rents were increased by more sooner (i.e. 4% in 2022/23 and 2% thereafter) this would further lessen the impact on the deficit. If rents were to be frozen for a second year in a row (2022/23), a minimum annual increase of 3.3% would be required over the following three years before returning to 2% annual rent increase.

4.9.2 **Reduce revenue expenditure –** The Housing Service Improvement Plan already assumes a 12% reduction in annual expenditure by 2025/26. Detailed forecasting is currently taking place to map out where and when savings will be achieved. This is already an ambitious improvement programme. It is therefore not realistic to assume that a further reduction in revenue expenditure could be achieved through efficiencies alone. Service reduction would therefore need to be considered - £2m equates of around a fifth of the annual staff budget for the HRA.

4.9.3 **Reduce capital investment –** Whilst the budget motion proposed that the rent freeze be paid from contingency and reserves, unless income was increased or revenue expenditure reduced and sustained, this is not a one-off contribution. Capital investment funded from revenue is used to reduce capital borrowing requirements. £2m could support approximately £35m of capital borrowing which could enable 285 new social rented homes to be built or 1,000 homes to receive whole house retrofit (near EnerPhit standards) to help the Council achieve this net zero carbon target.

4.9.4 **Elongate the Capital programme –** The 2021/22 HRA Budget Strategy set out a capital investment plan that sought to build 10,000 new council led homes by 2027, achieve net zero carbon by 2030 and bring existing homes and neighbourhoods up to similar standard of new build over the next 20 years. For example, if the modernisation of existing homes and neighbourhoods was delivered over a 30-year period, instead of 20 years, this would substantially reduce borrowing requirements over the first ten years of the business plan.

4.10 The HRA Business Plan is reviewed annually. The options set out above will inform consultation with tenants on the 2022/23 budget, 10-year capital investment programme and 30-year business plan.

5. Next Steps

5.1 The revised 2021/22 HRA budget will be reviewed and revised in response to the latest Covid-19 restrictions and government guidance. Updates will be reported through regular monitoring reports to Finance and Resources Committee at Periods 3, 6 and 8.

5.2 The annual review of the HRA Business Plan will begin in the first quarter of 2021/22. Assumptions will be benchmarked against peers and where relevant, include market and industry standard projections, considering short and medium impacts of Covid-19 and Brexit. The contingency options set out in 4.9 will inform the review and consultation with tenants on the 2022/23 budget, 10-year capital investment and 30-year business plan.

6. Financial Impact

6.1 Appendix 1 sets out the revised 2021/22 Housing Revenue account budget. This includes the reduced income as a result of the rent freeze, an increase of £0.167m to fund the additional resource of two surveyors and one case officer to accelerate the work of the MTIS, an increased debt servicing costs to support the accelerated capital investment, and a reduction in Strategic Housing Investment Fund to balance the budget.

6.2 The detailed HRA Capital Programme 2021/22 being considered by committee sets out the acceleration of common stair improvements (including upgrades to windows, walls, ceilings, balustrades and handrails, stair painting, and improved lighting) and the HRA contribution to the additional capital works generated by the expansion of the MTIS team.

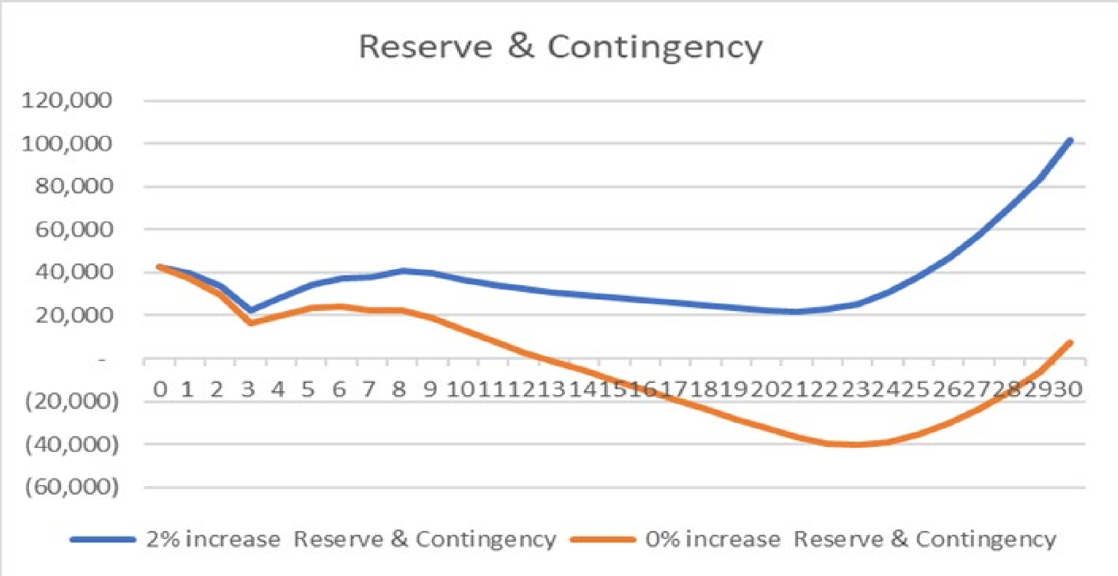
6.3 HRA reserves are contained within the Strategic Housing Investment Fund, an amalgam of the Repairs and Renewals Fund and the Council Tax Discount Fund. Income in excess of annual operating expenditure can be used within the same year to fund new capital investment (CFCR), repay old HRA debt or mitigate unforeseen risks. It can also be transferred to the Repairs and Renewals fund to support capital investment in future years. The draft budget assumed £12.140m would be available for strategic housing investment in 2021/22; as a result of the increase in costs due to acceleration of common stair works and MTIS and a reduction in income due to the rent freeze, this has now reduced by £2.199m to £9.941m.

6.4 A ring-fenced contingency was established in 2017/18 to mitigate the impact of further decreases in income and/or unexpected increases in expenditure. The contingency reserve was projected to be £11.5 million at the beginning of 2021/22, rising to c.20% of the annual income by 2027.

6.5 A one-year rent freeze means a reduction of £2.014m in projected gross rental income in 2021/22, or £1.939m in net income. Unless income is increased in future years to compensate this equates to a £93.921m reduction over the lifetime of the business plan. It also increases the overall deficit by 179% from £25.300m to £70.594m, lasting two years longer (2029/30 – 2043/44).

6.6 The proposed budget (funded by a 2% rent increase), projected an average annual deficit of £1.9m over these 13 years. However, it is important to note that the deficit only related to in-year expenditure exceeding income and there was enough in reserves to completely offset it. Whilst there is enough in reserves in 2021/22 to cover this loss income, the reduction of c.£2m revenue income year after year means that there will be less reserves and contingency built up prior to the deficit years and greater in-year deficits to be offset during the deficit period. Once reserves are exhausted, the contingency would be called on to seek to balance the budget. The combined effect of the rent freeze means the reserves and ringfenced contingency are exhausted by year 13 (five years into the deficit period), only recovering in year 30 of the plan.

6.7 The graph below sets out the impact on reserves and contingency as a result of the rent freeze.



7. Stakeholder/Community Impact

7.1 Each year the views of tenants are sought on the HRA budget strategy, investment plan, services and associated rent levels. There is a regular programme of tenant engagement and customer insight. This includes regular satisfaction surveys, focus groups, tenant panels, tenant led service inspections and scrutiny, resident and community meetings and annual budget consultation.

7.2 Consultation on the 2021/22 budget took place in 2020. With Covid-19 distancing restrictions, most of the budget consultation took place virtually, including a phone and online survey, social media campaign and an online meeting with Edinburgh Tenants Federation (ETF) members. All tenants received a paper copy of the budget consultation as part of the Tenants' Courier newsletter during the consultation period.

7.3 The annual Tenants' Survey is carried out by an independent third party, procured by the Council. The Council provides a random sample of tenants contact details, weighted by locality. This year, due to Covid-19, the survey was carried out via phone between July/ August 2020 and completed 1,000 surveys (a statically robust sample size). The survey is broadly representative of previous surveys and the overall tenant group. Tenants were surveyed from all property types and from all localities. The gender split and age range of survey respondents is also representative of our overall tenant group.

7.4 This year's consultation sought tenants' views on the changing focus of the investment strategy from investing in the interiors of homes, to buildings and neighbourhoods. While improvement inside tenants' homes and external fabric of buildings remain priority areas for investment, over half of the surveyed tenants said more investment should be made to improve common areas including safe, modern stairwells, improved waste management and recycling facilities, as well as, access to green open spaces and local shops. One in three respondents also cited improved transport links, sports facilities, community meeting spaces and access to community growing spaces as priority areas. 76% of tenants confirmed support for the investment plan funded by a 2% rent increase, with a further 22% supporting increasing rents beyond 2%, if priorities could be delivered more quickly.

8. Background reading/external references

8.1 Housing Revenue Account (HRA) Budget Strategy 2021/22, Housing, Homelessness and Fair Work Committee, 5 November 2020.

8.2 Housing Sustainability Update, Housing, Homelessness and Fair Work Committee, 5 November 2020.

8.3 HRA Budget Strategy 2021-31, City of Edinburgh Council,18 February 2021.

9. Appendices

9.1 Appendix 1 – Housing Revenue Account – Revenue Budget 2021/22 (Revised)

Appendix 1 – Housing Revenue Account Budget 2021/22 (Revised)

	Projected Outturn 2020/21 £m	Proposed Budget 2021/22 £m	Movement £m	Movement %	Note
Net Income	**103.138**	**102.699**	**-0.439**	**-0.43%**	1
Expenditure					
Housing Services	33.249	34.100	0.851	2.56%	2
Property Maintenance	19.638	21.009	1.371	6.98%	3
Covid-19 Extraordinary costs	3.316	0.000	-3.316	-100.00%	4
Debt Charges	36.337	37.649	1.312	3.61%	5
Strategic Housing Investment	10.598	9.941	-0.657	-6.20%	6
Total Expenditure	**103.138**	**102.699**	**-0.439**	**-0.43%**	

Note 1. - "Net Income" is the total rent due, less written off former tenant arrears and rent loss due to empty homes. It also includes service charges and costs recovered in relation to communal heating schemes and owner occupiers. The net income due to the one-year rent freeze is reduced to £102.699m. The shortfall of £1.939m in net income (£2.014m gross rental income) is to be offset using the contingency and reserves.

Note 2. - "Housing Services" includes core housing management services, new tenant and community services like energy advice and tenant discount scheme. It includes employee costs, central support costs and recharges, premises and other expenditure. The revised budget also includes £2.0 million for the continued development of the Housing Service Improvement Plan (HSIP), £1.0 million for the enabling work associated with large-scale regeneration projects and £0.167m additional resource to accelerate the MTIS pilot. An accumulated saving of £1.05 million (since 2019/20) has been included in the draft budget as part of the HSIP in order to reduce the total expenditure by 12% (£14.3 million) by 2025/26, which has been partly offset by the inflationary increase.

Note 3. - "Property Maintenance" includes responsive repairs, estates maintenance, routine gas servicing and the costs associated with bringing empty homes back into use. As in "Housing Services", an accumulated saving of £4.0 million (since 2019/20) has now been incorporated in the draft budget as part of the HSIP, which is partly offset by the "additional" repairs and maintenance for new homes and inflationary increase on estate management/maintenance expenditure.

Note 4. - "Covid-19 Extraordinary Costs" includes the additional costs (£3.316m) as a result of Covid-19 on operations. Significant adjustments have made to services to comply with government guidance and protect tenants and staff, including adjustments to buildings to manage social distancing, staff training, equipment and materials, staff shielding and absence due to ill health, allowances for extra time for cleaning, facilitating social distancing. No additional costs are currently assumed in the 2021/22 revised budget, but will be reviewed, and revised if appropriate, as part of the month three revenue monitoring. An increase in expenditure would reduce contributions to the Strategic Housing Investment Fund.

Note 5. - The HRA borrows to finance planned housing investment and house building capital programmes. “Debt Charges” are capital financing costs (principal repayments and interest). The 3.61% increase is in line with the capital investment plan set out in the 2021-2031 budget strategy report and includes the additional financing costs required to support the £1.86m accelerated investment for common stairwells refurbishment and the HRA’s share of the c.£4m mixed tenure improvement work brought forward by the MTIS additional resource. As a result of prudent treasury management, net debt levels are expected to have increased by only £27 million over the last five years, whilst delivering nearly £345 million of capital investment.

Note 6. - “Strategic Housing Investment” relates to income in excess of annual operating expenditure. It can be used within the same year to fund new capital investment (CFCR), repay old HRA debt or mitigate unforeseen risks. It can also be transferred to the Repairs and Renewals fund to support the new build programme in future years. The main reason for the reduction is the result of an increase in expenditure and a reduction in expected income as a result of the rent freeze. The Strategic Housing Investment Fund is an amalgam of the Repairs and Renewals Fund and the Council Tax Discount Fund.