AGENDA ITEM No:

Housing, Finance and Corporate Services Policy and Scrutiny Committee

City of Westminster

Date:	Monday 6th March 2017
Classification:	General Release
Title:	Housing Investment Strategy and Housing Revenue Account Business Plan 2017/18
Report of:	Barbara Brownlee, Director of Housing and Regeneration
Cabinet Member Portfolio	Councillor Rachel Robathan, Cabinet Member for Housing
Wards Involved:	All
Policy Context:	City for Choice / Heritage / Aspiration
Report Author and Contact Details:	**Jake Mathias – 0207 641 3359** **jmathias@westminster.gov.uk**

1. Executive Summary

1.1 This report presents the Housing Investment Strategy and thirty-year Housing Revenue Account (HRA) Business Plan. This is the fifth such plan since the introduction of self-financing in 2012. The City Council's investment plans are ambitious and will deliver a range of lasting benefits for the City, its residents and the City Council. They will allow the City Council to realise much of its 'City for All' ambitions of aspiration and choice; delivering new homes and leveraging the value of our land assets to bring forward investment in some of Westminster's poorer neighbourhoods.

1.2 Since last year the recommended budget for investment (including both capital and revenue) in the Council's existing stock has been increased from £1.4bn over thirty years to £1.5bn. In the light of the uncertainties created by welfare reform changes and the Housing and Planning Act 2016 (HPA), a prudent approach to budget setting was adopted last year and it was signalled that officers would revisit the plans at this time. A budget of £1.5bn is viable but minimum reserves are reduced to £10m, instead of £11m in two of the 30 years. This increase of c.£100m primarily relates to:-

- A revised 2% contingency allowance over the 30 year business plan period on major works to the existing stock; (c.£30m)
- Allowances to deal with contractor default and latent defects; (£4m)
- An anticipated increase in the number of units requiring void refurbishment works; (c.£8m)
- A re-profiling of capital expenditure as a result of new major works contracts; (c.£24m)
- New health and safety requirements; (c.£1.4m)
- One year's construction inflation from 2016/17 to 2017/18 (over 30 years). (£c.35m)

1.3 Key elements of the HRA capital investment programmes included are:

- Continued investment in existing housing stock (£1,034m);
- Investment in the housing estate regeneration programme (£509m);
- Other new supply schemes (£99m)
- Affordable Housing Fund expenditure on new supply over the 5 year period 2017/18 to 2021/22 (£114.37m including £58m on HRA schemes)

2. Key Matters for the Committee's Consideration

2.1 To consider the changes between the 2016/17 business plan and the 2017/18 business plan.

2.2 To consider the risk mitigations in Section 5.

3. HRA investment programme – expenditure on existing homes

3.1 The 2016/17 HRA Business Plan accepted that, because of the reduced income assumed as a result of Government rent changes, not all of the Council's housing stock would be able to be brought up to – or maintained at – the 'CityWest Standard'. Rather, a 30-year investment programme was set at £1.4 billion (£941m capital and £473m revenue), which would still enable the Council to meet the Government's Decent Homes standard.

3.2 Officers have continued to take a prudent approach to budget setting because of the on-going uncertainties arising from the HPA. However, following further review of necessary investment, an increase in the 30 year budget has been proposed as part of this year's Business Plan. Specifically, it is assumed that an additional c. £100m would need to be spent over the Plan period leading to a total projected spend of c. £1.5 billion (£1034m capital and £485m revenue).

3.3 Total expenditure on major works programmes in the first five years of the programme therefore amounts to c.£291m investment (capital and revenue), broken down as shown below.

Description	5yr Plan	30yr Plan
	£m	**£m**
Mechanical & Electrical	63	342
External	88	377
Major Voids	18	94
Kitchen & Bathrooms	8	68
Lifts	10	50
General	5	29
Fire precautions	14	38
Adaptations	6	36
Total Capital Improvements	**211**	**1,034**
Repairs & Maintenance	80	485
Total Investment	**291**	**1,519**

3.5 One of the key ways that CityWest Homes is seeking to ensure better investment and budget control is through its current procurement exercise. This involves long term service agreements with a limited number of contractors. CityWest Homes already has a 10 year term contract to provide responsive repairs works, but this is coming to an end in April 2017. The proposal is to grant a series of new contracts covering not just responsive repairs, but also major works. This will provide better value for money and drive a reduction in costs. As well as improved management a 2% (industry norm) contingency has been applied.

3.6 The contracts should mean that procurement is much more stream-lined with a shortening of the time period from project approval to 'start on site'. In the short-term, however, the procurement of the Term Contracts has meant that a number of projects have been delayed, to be captured under the new regime, which, along with the regeneration programme, is the reason for the higher capital investment profile in the first three years of the Plan.

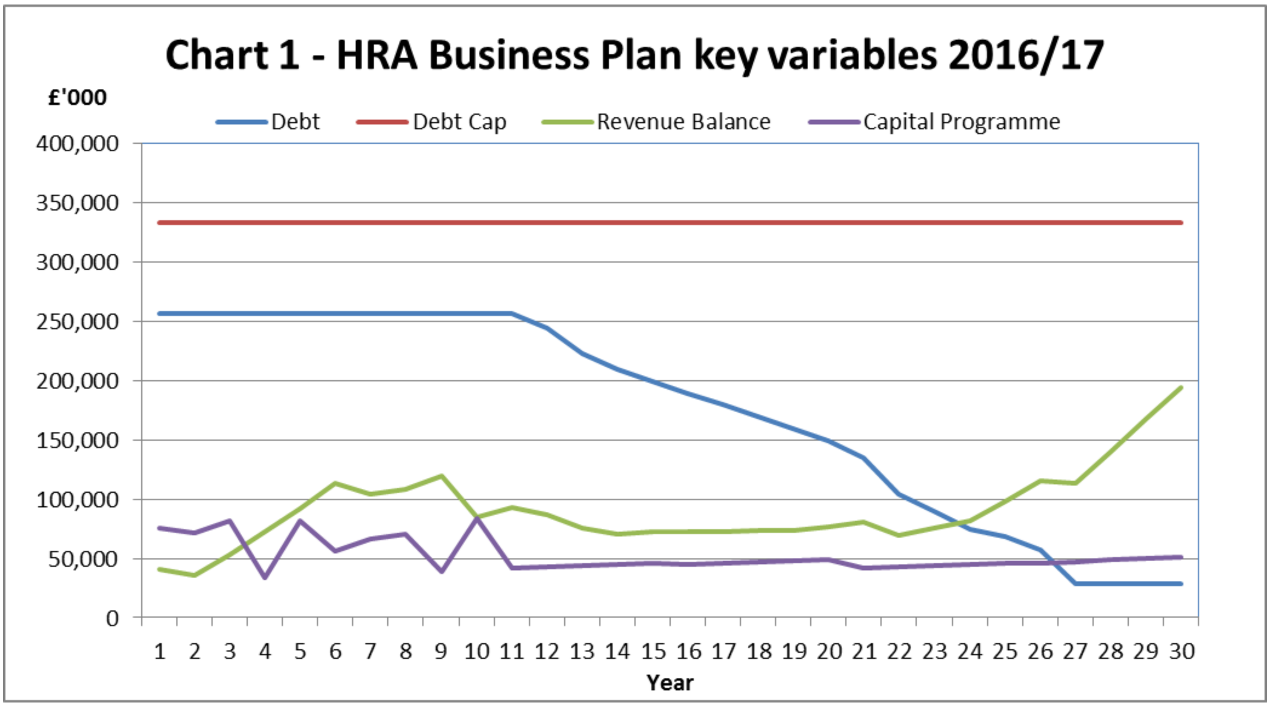
4. The HRA business plan base financial position

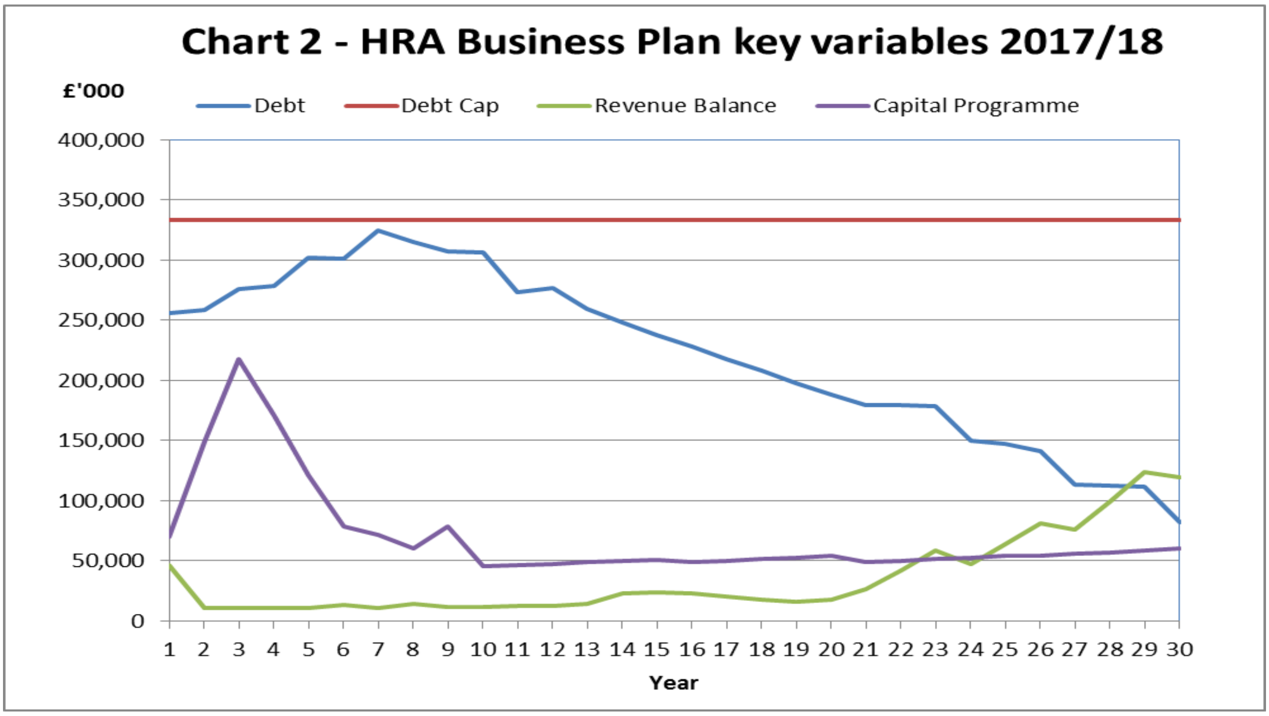
4.1 This report sets out the Council's Housing Revenue Account (HRA) Business Plan for the 30-year period 2016/17 to 2046/47. The base financial position will deliver the following:

- Investment in existing stock of £1.5bn, including major works capital expenditure of £1.034bn and revenue repairs and maintenance of £485m.
- Investment in new affordable housing of £509m generating 992 new HRA units, along with improved public realm and community facilities.
- Reduction in HRA debt in year 30 to £82m.
- HRA Revenue balances in year 30 of £120m.

- Efficiency savings of £5.2m in the first five years which are reinvested in service delivery.

4.2 The charts below show the key variables of last year and the current year's Business Plans: the debt cap (set by government under the self-financing settlement); the debt (total borrowing requirement); capital programme expenditure; and the cash reserves balance. Each of these is explained further below. This shows that the HRA can fund the regeneration and other identified investment opportunities, with support from additional capital grants and receipts.





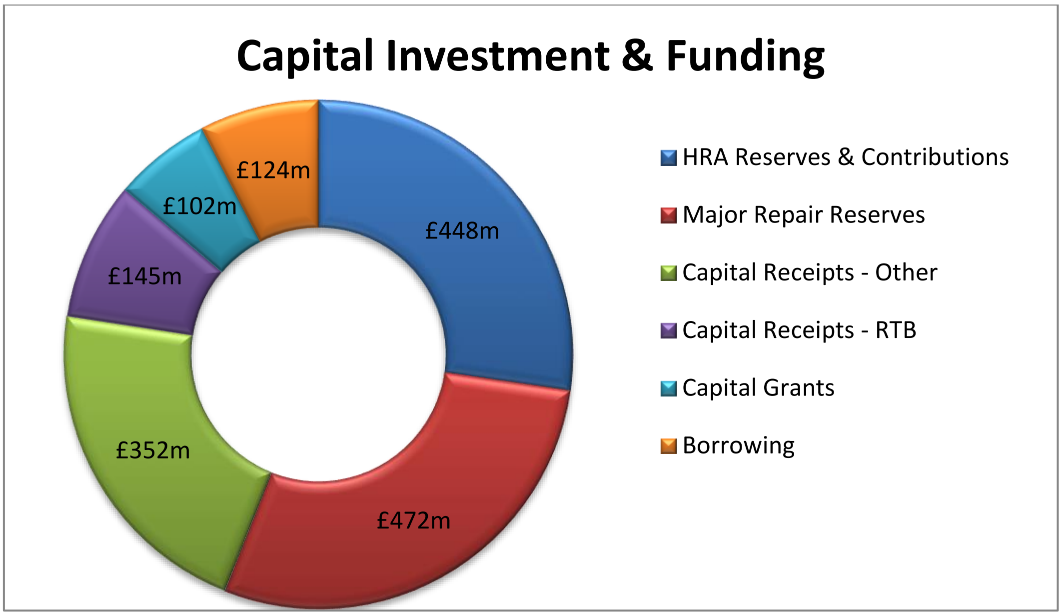
4.3 **Debt cap (red line)** - each local authority HRA has a debt cap, imposed by government as part of the 2012 self-financing settlement. This limits the amount of borrowing that the HRA can undertake. Westminster's cap was originally set at £325m, but was increased in 2014/15 to £334m. As the chart shows, the borrowing limit remains the same over the 30 year period so the maximum amount the HRA can borrow is in line with government rules.

4.4 **Debt (blue line)** - As the chart shows, the Council is able to fund the investment programmes outlined in this report with additional borrowing. Borrowing peaks in Year 7 and reduces thereafter as most of the regeneration scheme are completed or near completion. The plan assumes that maturing debt will be re-financed as long term loans expire and where resources allow, the principal sums are progressively repaid. Debt levels are higher than that presented last year in the first 14 years because of the additional expenditure planned on maintaining the existing stock and increased expenditure on regeneration as shown by the rising blue line from year 1 to year 8 and its fall back to around £250m in year 14. This compares with the flat line at around £250m in last year's projection. Borrowing is estimated to fall from £256m to £82m (£29m last year) over the life of the plan resulting in a net debt repayment of £174m (£228m last year) over the 30 year period. The borrowing headroom is estimated to improve from £78m (£77m last year) to £252m (£305m last year) at the end of the plan providing future investment capacity in the later years of the programme. The reduction in headroom of £53m compared to last year's plan enables the HRA to access the additional borrowing required to fund the regeneration projects.

4.5 **Revenue balance (green line)** - A minimum reserves balance of £11m has been assumed in the plan as a contingency against unexpected expenditure and to mitigate potential risk. This largely arises from the dependency upon capital receipts which are dependent upon delivery of the regeneration programme and the continued buoyancy of the property development market. This continued level of reserves in this year's programme is felt to be prudent in light of the future uncertainty around Brexit, Government housing policy, rent policy, inflation, interest rates and cash flow. As the charts shows, the revenue balance is estimated to rise from £46m to £120m over the life of the plan. However, last year's plan saw balances rise from £40m to £194m. The balances are close to the minimum from year 2 to 10 then slowly increases thereafter as regeneration projects are completed or near completion. The reduction in balances of £74m from last year's plan have helped fund the higher capital programme.

4.6 **Capital programme (purple line)** - Total planned capital investment in the HRA totals £1.6bn (£1.2bn last year) over 30 years. This includes major works on existing stock of £1bn (£933m last year), regeneration £509m (£248m last year) and other new supply schemes £100m (£49m). The programme is estimated to rise sharply and peak in year 3 as a result of increased regeneration expenditure, then gradually reduce over the next 7 years and stabilise from year 10 onwards as the regeneration projects are completed or near completion. The amount of HRA expenditure on regeneration has increased compared with last year and it also happening earlier, hence, the large peak in expenditure in year 3 to 6.The higher regeneration programme will deliver 992 new affordable homes.

4.7 This will be funded mainly from: Reserves & Contributions of £448m; capital receipts of £352m generated from land and market sale of new homes; capital grants of £102m; RTB sales receipts of £145m, and borrowing where appropriate. This is shown in the chart below.



Key Business Plan assumptions

4.8 The key assumptions that underpin the business plan are set out below.

4.9 **Housing stock** – the Plan is based on a forecast of reducing tenanted stock numbers from 12,054 at the beginning of year 1, to 11,103 in year 30. This includes a total 992 new units, 765 RTB sales, 688 demolitions and 250 high value void sales.

4.10 **Dwelling rents** - average weekly rent per property is estimated to increase from £124.26 to £227.20 in year 30 of the plan. This reflects the 1% rent reduction in the first four years to 2019/20 in line with government regulation and an estimated 3% average rent increase for the next five years up to the end of the original 10 year rent policy. For subsequent years a prudent inflationary increase is assumed as Government rent policy beyond the initial 10 years rent policy period is still uncertain.

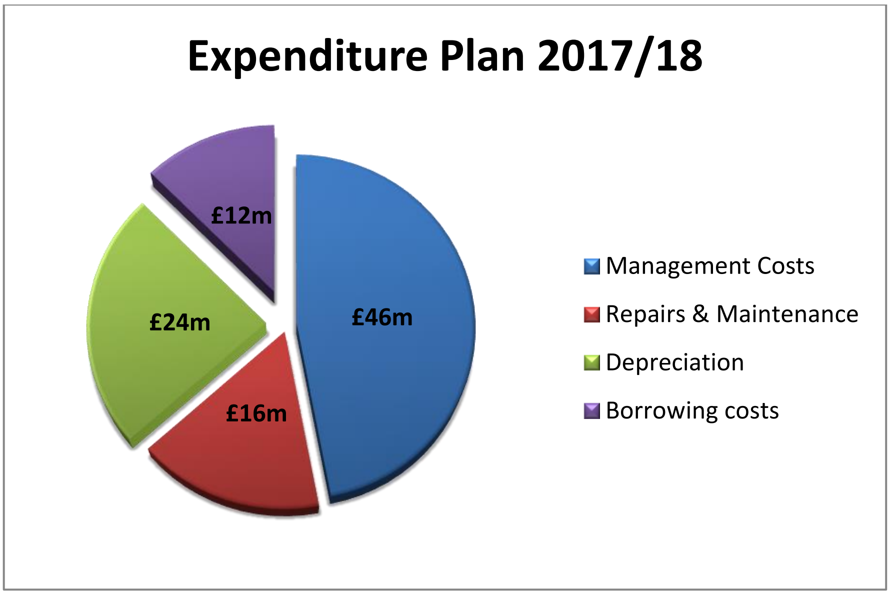
HRA stock movement

Tenure	Tenanted	Affordable / Intermediate	Leasehold	Total
Stock numbers at 01/04/2016	12,054	0	9,098	21,152
Additions	518	474	0	992
Demolitions	-454	0	-234	-688
Disposals - RTB	-765	0	765	0
Disposals - HVV	-250	0	0	-250
Stock numbers at 31/3/2046	**11,103**	**474**	**9,629**	**21,206**

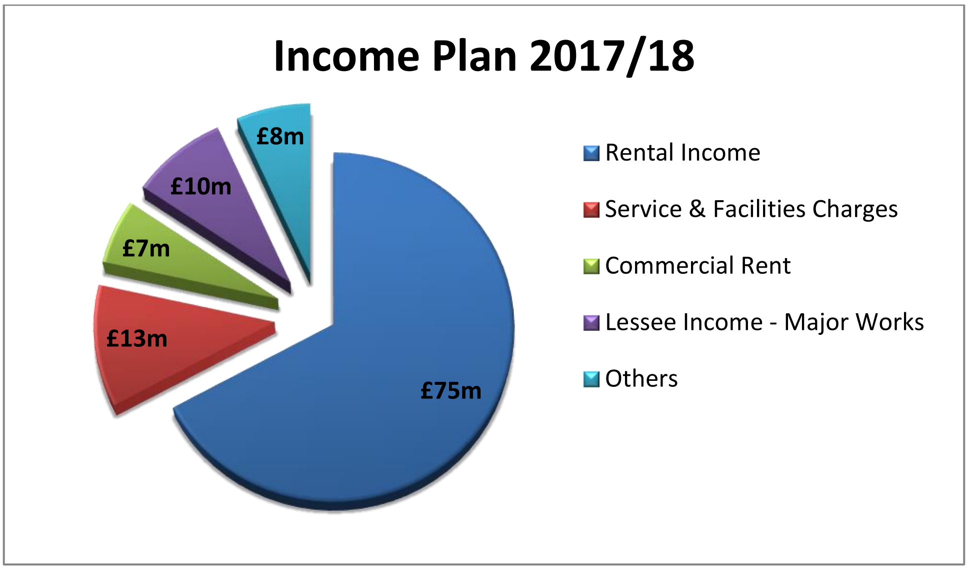
Assumed rent increases

Year	Year	Average Rent per week	Assumed Rent Increase	% (Decrease) /Increase	ent Increases
1	2016.17	£124.26	-£1.19	-1%	-1%
2	2017.18	£123.07	-£1.19	-1%	-1%
3	2018.19	£121.88	-£1.19	-1%	-1%
4	2019.20	£120.70	-£1.18	-1%	-1%
5-9	Annual increases in line with CPI +				1%
10-30	Thereafter annual increases in line with CPI +				0%

4.11 **Management Costs** – the chart below show the operating account expenditure for 2017/18. The total annual expenditure is £98m, the bulk of which is the housing management and service costs of £46m. £38m of the management costs represents direct estate management services for tenants and lessees delivered through City West Homes (CWH) and other providers, and support services delivered thorough other Council services. The balance of £8m consists of other costs such as communal heating & hot water provision and other estate services which are recoverable from tenants and lessees.



4.12 The chart below show the operating account income for 2017/18 in the Business Plan.



4.13 Being a 30-year plan, the HRA Business Plan is based on a number of assumptions about the future. We have been prudent in setting these assumptions so that risk is minimised. The key assumptions used in the plan are shown below. See section 5 for a discussion on how risks are managed.

Risk area	Assumption	Comment
Inflation	RPI at 2.5% CPI at 2%	Assumed long term inflation for planning purposes applied to expenditure items.
Rent policy	Y 1-3 1% reduction Y 4 – 9 CPI +1% Y10+ CPI only	A conservative approach to rent increases as local authorities have flexibility under the self-financing regime.
Void rates	1.5%	Assumed long term void rate for planning
Bad debt provision (BDP)	1.5% from Y2 onwards	Assumed long term BDP rate for planning
Interest on debt/balances	0.5% on balances; 4% on new and rescheduled debt	Reflects current rates available and historic evidence.
RTB Receipts	30 in the first three years, then 25 thereafter.	Best estimate based on historical sales trends and expressions of interest
Minimum cash balances	£11m	Approximately 10% of turnover. Prudent in light of current economic and market risks as a result of Brexit.
High Value Voids (HVV) - The HPA requires housing authorities to	250 sales over 3 years.	It is assumed the levy payment will be funded from capital receipts from units sold.

Risk area	Assumption	Comment
sell interest in any vacant higher value (HRA) housing and pay a levy to government		

4.14 Based on these assumptions, the business plan remains viable over the 30-year period; and the investment programmes are deliverable.

5. RISK MANAGEMENT

5.1 As the HRA headroom and financial capacity is fully utilised by the increase in the proposed capital programme over the immediate planning period the ability of the HRA to absorb and manage risk is reduced as HRA reserves will be at minimum levels.

5.2 This means that if any overspends occur or capital receipts are delayed or reduced this would necessitate mitigation through a range of management actions as the HRA is legally unable to run deficits.

5.3 The range of management options available within the HRA to mitigate any additional risks are as follows:-

1. Reduce expenditure
   i. Reduce major works capex (e.g. from £1.5bn to £1.4bn over 30 years).
   ii. Reduce Major works capex over the first ten years (when capex peaks).

2. Re-profile, extend or delay expenditure
   i. Programme the regeneration spend so that schemes run sequentially rather in parallel or delay either some projects within Church Street or Ebury.
   ii. Reprofile major works capex over the first ten years (when capex peaks).
   iii. Reprofile and extend regeneration scheme programmes.

3. Dispose of HRA assets
   i. Identify surplus assets or sell additional HRA properties (the average value of a dwelling is approximately £500k)

4. Vary HRA or Affordable rents

5. Increase funding from the Affordable Housing Fund (AHF)
   i. The risk of increases in cost for the acquisition of affordable housing can be met from the AHF fund through reprioritisation of funding c£40m.

6. Lobby for an increase in the debt cap.

5.4 An analysis of the current regeneration capital programme shows that after excluding schemes that are either cash limited or contractually committed and excluding spend on new affordable acquisition where the affordable housing fund would pick up any potential increase in cost risk that an appropriate level of risk contingency of c.£50m has been provided for.

5.5 As noted in section 4 above, the base business plan uses prudent assumptions so that risk is minimised. Set out below is a summary of other potential risks to the stability of the business plan. Quarterly governance meetings are held between senior officers and elected officials, at which programme performance is reviewed and risks monitored.

Risk	Impact	Mitigation
Capital Receipts: The plan assumes estimated capital receipts of £352m will be recovered and used to fund the development of new homes.	Any significant slippage in the recovery of these receipts may pose a cash flow risk for the HRA.	Robust monitoring of the timing of the receipts will help inform management action to mitigate this risk. Management options identified above would need to be applied.
Rent Policy	If rents were to increase annually by CPI after 4 years, not by CPI+1% as modelled, the impact would be a cost of c. £330m and the plan would be unviable.	Management options above would need to be applied.
Interest rates	If interest rates were to rise to 6% the impact would be a cost of c. £62m. But the plan would still be viable.	Management options identified above would need to be applied.
Inflation	If RPI inflation were to increase above that assumed by 1% the impact would be that the Plan will no longer be viable. But the increase in costs would be partially offset by increased income as this is also based on CPI inflation.	Management options identified above would need to be applied.
Capital Costs	If the cost of construction and professional fees on the regeneration programme were to increase by 20% this would cost £50m.	This is provided for within the scheme budgets.
Welfare Reform: Implementation of Universal Credit, benefit cap and other welfare reform changes.	May increase rent arrears which impacts HRA income.	Robust monitoring of service activity and the HRA Business Plan.
Brexit - Adverse impacts on costs and values as a	There is increased uncertainty about the costs of projects due to changes in the cost of materials and labour arising	A selection of current projects are being reviewed to identify and seek to quantify the impacts based on the best

consequence of Brexit	from changes in the value of the pound relative to other currencies. Equally there are changes in the attractiveness of London as a residential investment, positively due to falls in the value of the pound and negatively from lack of access to Europe. These are highly uncertain and may lead to increased caution on the part of contractors and developers when bidding for work or assessing the risks/rewards of current projects.	evidence available to highlight areas where further measures need to be taken.

6. FINANCIAL SUMMARY

6.1 This report relates to the Housing Revenue Account (HRA) Business Plan and overall Housing Investment Strategy. It is based on 30-year period. It has been updated to reflect the current position including the impact of known Government policies, funding arrangements and risk factors. All expenditure and income are included in Council budgets.

6.2 The capital programme proposed will see an increase in capital spend. The gross HRA capital expenditure required to deliver the plans within this investment strategy is £700m over the next five years. This will rely upon funding of £210m of HRA revenue resources, £381m from RTB & Other capital receipts, £58m from the Affordable Housing Fund and £52m of new borrowing or grant.

6.3 The funding of this programme is largely dependent upon the timing and value of asset disposals that underpin the regeneration programme.

6.4 Once these HRA funds are committed they will utilise all of the foreseeable headroom and financial capacity within the HRA. It will result in the HRA reserves being at around a minimum level of c.£11m for 20 years and borrowing peaking at £334m in year 7. This will limit the ability of the HRA to contribute major funds to any further housing development until around year 10, therefore the Strategic Housing Options study currently underway, is seeking alternative methods to build more homes.

6.5 As the plan repays debt the headroom will increase from year 7 and by year 13 the revenue reserves will also start to increase, which will allow for further new investment to begin again at this stage.

6.6 As the HRA is legally not allowed to run a deficit this means that if there is an overspend on the capital programme or elsewhere, or if capital receipts are reduced or delayed, the options available to contain these pressures will necessitate either reducing, reprofiling or stopping expenditure on the capital programme or realising funds through the disposal of HRA assets, or applying more funding from the AHF. These options are identified within the risk management section above.

6.7 There remain a number of uncertain risks identified including interest rate, inflation and the impact of Brexit that will require close monitoring and the adoption of a range of management mitigations if they adversely impact upon the HRA.

6.8 The reduction in the capacity of the HRA and the potential impact of risk factors requires a strong risk mitigation strategy that can be quickly adopted if any of adverse risks materialise. The range of management options available to mitigate risk are outlined in detail.

6.9 The latest 30-year HRA Business Plan demonstrates that the investment proposals are fundable, subject to the assumptions within the plan, and that the HRA remains a sustainable and viable entity over the thirty year period.