



Additional / To Follow Agenda Items

This is a supplement to the original agenda and includes reports that are additional to the original agenda or which were marked 'to follow'.

Nottingham City Council Audit Committee

Date: Friday 6 May 2022

Time: 2.30 pm

Place: Ground Floor Committee Room - Loxley House, Station Street, Nottingham, NG2 3NG

Governance Officer: Kate Morris **Direct Dial:** 0115 876 4353

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Audit Committee – 6 May 2022

Title of paper:	External Review of Housing Financial Management and Council Response	
Director(s)/ Corporate Director(s):	Sajeeda Rose	Wards affected: All
Report author(s) and contact details:	Kevin Lowry, Interim Director of Housing.	
Other colleagues who have provided input:	Clive Heaphy, Corporate Director, Finance and Resources Beth Brown, Head of Legal and Governance	
Recommendation(s):		
1	Audit Committee note the issues and recommendations agreed by Executive Board on 28 April.	
2	Audit committee note and take assurance from the summary of Council Response and action in progress and being developed.	

1 Reasons for recommendations

- 1.1 The Executive Board received and approved a report on 28 April 2022 recommending the in-sourcing of the Council's housing management functions. including reports for Richard Penn and Cipfa (appended). This report highlighted the updated position and revised quantum in regard to the unlawful misuse of Housing Revenue Account funds and the Councils Response to the issues raised in the two reports. This was a progression from the issues exposed and raised in December 2021 and considered by Full Council on 4 January 2022.
- 1.2 The Executive Board paper contained 12 recommendations which included proposals to
- 1.2.1 establish the exact level of misused funds and to seek Ministerial approval to pay back to the HRA up to £40m from the general fund.
 - 1.2.2 serve notice on NCH to terminate the arms-length management agreement and to bring Council housing management functions back into direct management. This included extensive engagement with tenants and staff at NCH.
 - 1.2.3 note that there will be an impact on the MTFP 2023-2023-2025/26.
 - 1.2.4 enhance short-term governance to protect the HRA and ensure that the recommendations of the Penn and Cipfa reports are achieved.
 - 1.2.5 Approved a transition programme budget of £750k.
- 1.3 All recommendations were accepted in full and a detailed programme of actions is in progress or being developed.

2 Background

- 2.1 A review commissioned by the Council had identified that NCC, including through its arrangements with NCH, has acted unlawfully in relation to breaches of the HRA Ring Fence.

- 2.2 The issue was previously reported to and considered at an Extraordinary meeting of Full Council on 4 January 2022. Amongst other actions agreed, two further reports were commissioned. This paper addresses key points arising from the findings of these two reports by an independent investigator, Richard Penn and CIPFA (Chartered Institute of Public Finance and Accountancy).
- 2.3 The further work commissioned from Richard Penn and CIPFA, following the identification of initial breaches, has identified the causes of the unlawfulness and how it came about and that the scale of unlawful use of funds diverted away from the HRA is greater than first identified.
- 2.4 CIPFA's initial report identified the unlawful treatment by NCC of the NCH 'management fee rebate' which was valued at £14.367m. CIPFA's additional work has uncovered a further sum of up to £25.759m of detected and assessed issues taking the overall scale of the issue of up to £40.126m. This comprises:
- i) Issues raised in the original report concerning the unlawful treatment by NCC of NCH 'management fee rebates of £14.367m (35.8% of the total).
 - ii) Issues forming workstream A of CIPFA's review which concerned historical decisions taken by NCC without full consideration of the HRA ring-fence totalling £8.503m (21.2% of the total).
 - iii) Issues forming workstream B of CIPFA's review which concerned the extent to which HRA monies have been spent by NCH on non-HRA activities between 2014-15 and 2020-21 totalling £17.158m (43.0% of the total).
- 2.5 The investigations the council has commissioned have identified issues with historical financial mismanagement, a lack of adequate record keeping and governance failures that have occurred. Consequently, it is important that the council acts swiftly and decisively to deal with the matters raised to provide assurance to itself, tenants, taxpayers, the Improvement and Assurance Board and Government. Members will need to have confidence that officer and external auditor advice is robust and consequently that the council's accounting and use of HRA is legal and passes the 'who benefits' test to ensure that the impact of HRA monies are spent in accordance with the ring fence for the benefit of Council tenants.
- 2.6 As well as rectifying past omissions and learning lessons, a key focus looking forward is on ensuring that decisions are taken which makes sure that these unlawful events cannot happen again. This includes clarity of roles for those responsible for safeguarding the HRA ring-fence, clear performance and financial controls within the council and in relation to the management of NCH, close monitoring of spending in the HRA, improved governance including enhancing the role of scrutiny and clear records to support future decisions around spending within the HRA.

3. The Council's response

- 3.1 The Council accepted in full the recommendations made at the Extraordinary Council Meeting on 4 January 2022. The Council commissioned further reports which are integral to the recovery process that the Council has embarked upon.
- 3.2 It is of deep concern that notwithstanding the seriousness of the issue, as evidenced by the service of a Section 114 Notice, a Section 5 Notice and exchanges of

correspondence between the Chair of the Improvement and Assurance Board and the Minister in relation to the HRA issue, that CIPFA, as part of their most recent work, have reported that they have seen no evidence of measures to properly separate HRA and non HRA funding and expenditure. As a result, the Council cannot be sufficiently assured that the HRA ring fence is appropriately protected.

- 3.3 The findings and recommendations contained in the reports (Penn and Cipfa) are evidence based or founded on the most reasonable assumptions that could be made at the time. For this reason, officers strongly advised that the findings and recommendations of the Penn Report and CIPFA were accepted in full and implemented. The recommendations include rectifying the deficiencies identified and ensuring that future governance and financial controls are adequate and strengthened to protect the ring fence. The recommendations were accepted in full by Executive Board on 28th April 2022.
- 3.4 To achieve this, it will be necessary to re-create an effective NCC Housing Client Team and to strengthen the Council's technical and professional capacity and capability on HRA and Housing. The current year accounts (2021/22) and the MTFP will be impacted and this could result in a potential gap each year. This will be considered in due course via the appropriate governance routes and mitigated to ensure the financial stability of the council. There will be further work in regard to the values reported to ensure that the precise sum for repayment is identified.
- 3.5 Further the oversight of any future charges to the HRA will be undertaken by the Interim Director of Housing and the Senior HRA accountant who will both act as "HRA Champions" for the Council and provide that required assurance to the Council regarding the future management of the HRA. As part of broader tenants and member involvement in relation to the council housing function of NCC, the Council will establish governance and oversight arrangements in relation to the HRA for members and tenants that are based on best practice in the sector. In addition, the Council will strengthen the role of the Council's Scrutiny arrangements to strengthen the overall governance arrangements covering the management of housing and the HRA.
- 3.6 Recommendation 6 is to bring the Housing Management function back "in-house" by service of 12 months' termination in accordance with Clause 59.3 of the 2020 Partnership Agreement. This will mean the return to the Council of the direct management of council housing from the expiry of that notice. This can be effected earlier by agreement between the parties. The aim will be to complete this work by 31st March 2023 to align with financial years.
- 3.7 This process will include undertaking the necessary due diligence and project planning to bring housing management staff into the council, address and where appropriate transfer contracts, resolve issue relating to assets and balance sheets and ensure that existing housing management and services remain the same for tenants. NCC will remain as the landlord.
- 3.8 This will also include making any changes that may be necessary to the Articles of Association of NCH and Board appointments in the interim period
- 3.9 The project will incorporate the necessary engagement and communications work to reassure staff and tenants. The Penn Report firmly recommends that in order for the Council to be able to demonstrate the necessary level of assurance over the use of HRA funds and during the transitional phase there will be a requirement for strengthened financial management, together with appropriate transition management

arrangements to provide in improved level of assurance in the management of the HRA.

- 3.10 It should be noted that the Together for Nottingham Plan already includes an action to review Council companies and subsidiaries. Progress on this issue will be monitored by the Companies Governance Executive Committee.

4. Technical steps to manage the transfer of functions

- 4.1 It should be noted that there is no recommendation from the Penn Report or CIPFA to enter into a full options appraisal. Where there is unlawful activity in regard to HRA and in the context of the existing Together for Nottingham Plan to address other financial issues, the Council needs to act decisively and quickly for the benefit of tenants.

- 4.2 To terminate the agreement with NCH notice should be served under 59.3 of the 2020 Partnership agreement which states:

“The Council will be entitled to terminate the Agreement at any time on giving not less than 12 months’ written notice to the Organisation.”

- 4.3 At the expiry of the notice period (or sooner by agreement) the service would be transferred to the council by a “lift and shift”. This means that the staff involved in day-to-day delivery will continue to provide customer service and tenants and leaseholders will experience a seamless transition.

- 4.4 A detailed project plan will be developed that includes, but not limited to:

- a) **Clarity of decision.** Why the agreement is being terminated and what NCC hope to achieve by in sourcing.
- b) **Governance.** Project Boards at various levels to oversee the project and to ensure engagement with key parties of tenants, leaseholders, staff, unions, stakeholders and contractors.
- c) **Resources.** There will need to dedicated capacity in particular in the areas of legal, finance (HRA), HR and communications. A budget of £750k to support NCC and NCH has been agreed.
- d) **Communications plan.** A detailed and timed communications plan aimed at all levels of engagement and progress including reactive capacity for press enquiries etc.,
- e) **Risk Register.** A detailed and RAG rated living risk register covering impacts on the Council as well as NCH. The risk to service disruption has to be mitigated.
- f) **Tenant engagement.** There will be an extensive engagement programme to develop how tenants will communicate with their landlord (rather than the landlords’ agent as at present).
- g) **Subsidiaries.** NCH have two subsidiaries. Careful consideration will be required in terms of the legitimate use in the future and protecting the benefits they provide for NCC e.g., provision of temporary accommodation.
- h) **TUPE.** The proposal is for a “lift and shift” which means that the service would transfer back to NCC intact. The workforce of NCH would transfer to NCC and the legal and practical engagement processes including consultation and engagement with unions and staff will be observed and commence early in the process.

- i) **Post transfer structure.** Building the council department that will bring together delivery services from NCH and strategic housing functions
- j) **HRA.** Dedicated resources are needed to implement the Penn and CIPFA recommendations.

4.5. The inaugural meeting of the internal project group is being held on Tuesday 3 May and the detailed plans will be produced. As indicated at item 4.4.2 there will be extensive governance of the project including oversight by the Overview and Scrutiny committee and the Companies Governance Executive Committee.

5. Actions to verify the CIPFA figures and process for repayment.

5.1 Further work will be undertaken, where appropriate, to validate CIPFA's extrapolated figures with a focus on future rather than past impacts. This will include further review into the values and justification of SLA's, and detailed analysis of the assets of NCH Enterprise and NCH RP. The objective is to mitigate the quantum but there is a risk that values of mis-used HRA could increase.

5.2 In regard to repayment to the HRA of misused funds the first £15m has already been set aside within General Fund reserves. A Ministerial direction will be required in order to repay monies to the HRA from the General Fund. However, we will first evaluate the level of cash at hand held by Nottingham City Homes and assets held by the two subsidiaries to see if the values can be mitigated by the transfer of cash and/or assets.

5.3 A new capitalisation request could be made if necessary but this would be a last resort after all other mitigations have been considered.

6. Published documents referred to in compiling this report

- Executive Board paper 28 April 2022
- Appendix 1 Richard Penn Report
- Appendix 2 CIPFA Report

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