Nottingham City Council: HRA Review Phase 2 – Workstreams A & B

Final Report

April 2022

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1. Executive Summary

Introduction

This report is a follow up to our HRA Phase 1 report that identified illegitimate breaches of the HRA ring-fence (subsequently confirmed by legal Counsel to be unlawful), namely payments made by NCH to NCC that were incorrectly credited to the General Fund (GF).

In this Phase 2 report, we set out our findings in relation to our work in following up on two of the recommendations in our Phase 1 report in relation to:

- Workstream A - Transactions between the HRA and the GF and whether decisions taken in relation to these transactions undermine the integrity of the HRA ring-fence, in particular we have focused on issues brought to our attention during Phase 1

- Workstream B - The extent to which HRA monies have been spent on HRA activities by NCH between 2014-15 and 2020-21

Workstream A

Our report on Workstream A is included as Part 1 of this report. In the production of this report we have examined information provided to us by NCC from both HRA and GF teams. The gathering of evidence has proven difficult. There is little or no “audit trail” (working papers, reports etc.) in relation to many of the issues considered and to support decisions that have been taken that impact on the HRA. This has necessitated both the use of estimates and extrapolation in order to arrive at an assessed financial position but in the absence of firm evidence, this is the only realistic approach.

Overall Conclusions

It is apparent that, historically, decisions that impact on the HRA have been taken by NCC without full consideration of the HRA ring-fence and have been presented as a fait accompli to those responsible for administering the HRA and that the basis for decisions and the supporting documentation was either not retained or quite possibly never existed.

On the basis of the evidence that has been provided to us and conversations with NCC staff in relation to this evidence, we conclude that a number of decisions have been taken that do not appear to be justifiable and appear to undermine the HRA ring-fence. In particular:

- Loss of income to the HRA on Manvers Street Car Park (£295,000)

- Cessation of Rebate in relation to RTB in relation to Public Realm Charges (£5,272,050)
- Introduction of a charge to the HRA in relation to Pest Control (£80,000)
- Charges in relation to Street Lighting (£2,272,420)
- Contribution from the HRA to the GF regarding Solar (PV) Panels (£400,000)
- Cessation of an HRA charge to the GF regarding the Housing Partnership Team (£183,560).

In total, the above items amount to **£8,503,030**. However, it should be noted that these amounts are based on historic values which may well have changed since the relevant decisions were taken.

In addition to the above there are other issues that we have examined where a firm conclusion cannot be made on the fairness of the charges made to the HRA since there is no clear basis or SLA on which these charges are based. In particular we would draw attention to the £500,000 charge that was introduced in 2019-20 for Corporate and Democratic Core. Whilst such a charge is common, no evidence has been provided to support the amount of this new charge.

There has been some work on developing SLAs undertaken (with NCH) but they do not seem to have the level of detail necessary to be a sound basis for calculating charges to the HRA and have not been finalised.

As we comment on a number of times in this report, it is essential that the amount and basis of all charges to the HRA can be properly justified in order to ensure the integrity of the HRA ring-fence.

Recommendations

We recommend that NCC considers our conclusions in relation to each of the items that combined have a value of £8,503,030 and determines:

- The amount the HRA should be reimbursed (taking into account any interest that might have accrued on the sums to be paid to the HRA)
- Any adjustments that might be necessary to reflect these amounts are based on historic values which may well have changed since the relevant decisions were taken.
- The actions needed to rectify these items from 2022-23 onwards.

We also recommend that work should be undertaken in relation to all charges to the HRA from the GF to provide a sound basis for the calculation of such charges combined with SLAs that have sufficient granularity to support these charges and any changes over time.

Finally, we recommend it should be mandatory that appropriate NCC staff with sufficient knowledge of the HRA ring-fence should be consulted before any decision impacting on the HRA is taken; ideally there should be an HRA “champion” who would need to agree to such decisions once satisfied such decisions do not breach the HRA ring-fence.

Workstream B

Our report on Workstream B is included as Part 2 of this report.

Key Findings

(a) **The funding from the ring-fenced HRA account received by NCH between 2014-15 and 2020-21 exceeded its spending on HRA activities**. Cumulative funding reached £417,800,920 by the end of 2020-21, whereas cumulative expenditure was £386,275,804. As a consequence, funding has exceeded expenditure by £31,525,117.

(b) **The scale of the gap does not take into account the annual payments made by NCH that NCC credited to the GF**. On the assumption that the £14,366,500 returned to the HRA, there remains a difference of £17,158,617 between HRA funding and HRA expenditure from 2014-15 to 2020-21.

(c) **The capacity for NCH to remedy this gap is constrained.** The cash balance of £15,673,588 at 31 March 2021 was essentially due to the net receipt of £22,759,590 in loans from NCC in 2020-21 for non-HRA projects. Whilst this cash inflow was to replenish NCH resources previously invested in non-HRA activities, the likely earlier utilisation of HRA funds on such non-HRA investments and the subsequent replenishment with non-HRA funds requires a formal direction from the Department for Levelling Up, Homes and Communities.

(d) **Furthermore, we have not seen any evidence that NCH has the appetite to ring-fence HRA funding and expenditure from its non-HRA activities.** Interviewees have emphasised that NCC has not placed any obligation on it to ring-fence HRA activities. Whilst some interviewees recognised a possible expectation that they should ring-fence HRA activities in future, we are not aware of how NCH has responded to NCC’s written notification of the need to do so.

(e) **The ledgers kept by NCH do not differentiate between HRA and non-HRA activities.** NCH was unable to produce a statement that summarised income received from the HRA and how it was utilised for each year between 2014-15 and 2020-21. Furthermore, NCH only maintained one ledger covering all of the activities and transactions of NCH ***and*** its subsidiaries in 2020-21, although this has since changed.

The consolidated financial statements for the group, and the financial statements for Nottingham City Homes Enterprises Ltd (NCHEL) and Nottingham City Homes Registered Provider Ltd (NCHRP) were dependent on a series of spreadsheet adjustments made at year end. The basis for the adjustments could not be readily explained or evidenced which in turn, complicates the process of demonstrating that the financial accounts comply with company law. Re-structuring account codes to differentiate between HRA and non-HRA activities, and maintaining different ledgers for each company within the group are critical and will require additional finance resources. This is required not only to enable HRA and non-HRA activities to be kept apart, but to mitigate the current reliance on one individual to explain the rationale of the existing working papers for the financial statements.

(f) **Separating HRA funding and expenditure within NCH has proved very difficult.** There is no direct linkage between the HRA funding received and how it has been utilised. As interviewees commented, all revenue funding received from NCC (HRA or General Fund), is treated as one income source. The main HRA revenue funding - the management fees and the maintenance and repairs fees are assigned to one account code and we have not found any journals or other papers to show how this aligns with the account codes used to record expenditure. In comparison, capital fees and works are assigned to specific cost centres. We have not been able to confirm with both parties that the funding from NCC recorded in NCH ledgers, aligns with the figures in NCC's records.

(g) **The difficulties in identifying how HRA funds have been utilised are compounded by out-dated recharges between account codes that we could not validate.** NCH are determining the costs of maintenance and repair works and capital works on non-HRA properties based on a schedule of rates that cannot be validated. The rates are bespoke to NCH, and there is no record of how they were compiled. Furthermore, the non-HRA costs recovered from NCH's subsidiaries are based on assumed costs per property rather than actuals and we have not been able to establish the basis of the estimates for overheads. This presents a strong likelihood that non-HRA subsidiaries could be subsidised with HRA funds which would be an illegitimate use of HRA monies.

(h) **We have not been able to adequately confirm the number of properties managed on behalf of the Council as specified in NCH's financial statements for 2020-21.** Regular reconciliations are not undertaken and there is a discrepancy of 65 properties that has not yet been resolved.

Overall Conclusions

In our opinion, the duty on NCC to ensure that HRA monies are only spent to the benefit of HRA tenants does not cease when it delegates the service provision to an arms-length management organisation. On the basis of our analysis, the failure to require its arms-length management organisation (NCH) to maintain this ring-fence for its operations means that, in addition to the £14,366,500 payments to the NCC General Fund that need to be remedied, a further £17,158,617 of HRA funds between 2014-15 and 2020-21 were not utilised by NCH on HRA activities by 31 March 2021. This estimate is based on the assumption that NCC funding reconciles with the records held by NCH.

Recommendations

NCC should, as a matter of priority, revise existing funding agreements with NCH to specify an obligation to ring-fence HRA activities. This should include the production of an annual statement that shows the funding received and how it has been utilised. This will necessitate changes in the accounting ledger(s) within NCH and is likely to require additional finance resources in order to make the change and to maintain future accounting records.

Having established the extent of HRA funding that has not been utilised for HRA activities, the Council will need to determine whether NCH has the capacity to remedy this matter without financial support. On the basis that the cash balance at 31 March 2021 largely comprised General Fund loans from NCC that replenish the highly likely utilisation of HRA cash surpluses to forward fund non-HRA investments, any such support would need to be approved by the Department for Levelling Up, Homes and Communities.

Alongside the actions to introduce an HRA ring-fence, the basis of costings and recharges for work done by NCH and its subsidiaries needs to be updated. The onus should be on actuals rather than estimates. For example, the schedule of rates is no longer fit for purpose and the cost of work done by the Construction Repairs and Maintenance team should be based on the materials and labour costs incurred, plus an overhead rate based on all indirect costs within the organisation. A similar approach should be used for all other services provided to subsidiaries and other organisations.

Part A: Workstream A Report

2. Introduction

Background

The focus of Phase 1 was the nature of the payments made by Nottingham City Homes (NCH) to NCC since 2014-15. NCC is dealing with the conclusions drawn in relation to this series of payments and the consequences for NCC and NCH.

In addition, however, the Phase 1 report identified the potential for further breaches of the HRA ring-fence in two specific areas which will be the focus of the Phase 2 work.

The Phase 1 report states, in Section 8, in relation to potential breaches of the HRA ring-fence within NCC:

Potential Breaches of the HRA ring-fence

It has been suggested to us decisions have been taken by NCC that could be challenged as having undermined the integrity of the HRA ring-fence. These decisions fall into two key categories:

- Decisions that have resulted in a loss of income to the HRA to the benefit of the GF;
- Decisions that have resulted in the HRA bearing disproportionate costs to the benefit of the GF.

An example of the former is a car park on HRA land for which it receives no income, the income going to the GF. We understand this has been the case for at least a decade.

An example of the latter is cessation of a rebate on the cost of public realm (including grounds maintenance, street lighting, and street cleaning) charged to the HRA by the GF to reflect Right to Buy (RTB) properties on council estates.

We have been provided with a schedule of more than a dozen such issues which will require further investigation. NCH is not party to these potential breaches of the HRA ring-fence.

The examination of the issues raised during our Phase 1 work are the subject of this Phase 2: Workstream A Report.

Work undertaken

In the production of this report we have examined information provided to us by NCC from both HRA and GF teams. The gathering of evidence has proven difficult. There is little or no "audit trail" (working papers, reports etc.) in relation to many of the issues considered and to support decisions that have been taken that impact on the HRA.

This is despite great effort on the part of the NCC staff consulted in the course of our work though the lack of evidence has been exacerbated by the apparent lack of capacity within NCC Finance teams.

However, on the basis of the evidence that has been provided to us and conversations with NCC staff, this report sets out our conclusions (where possible) on the issues raised in Phase 1 of our work. Inevitably, we also identify further work that needs to be done to ensure that the HRA ring-fence is maintained.

In examining the issues raised, we have taken into account the MHCLG's 2020 guidance on Operation of the HRA ring-fence (Annex A) together, where appropriate with any earlier guidance in relation to the HRA (namely Circular 8/95).

In this report we have grouped the issues by service area:

- Section 3: Resident Services
- Section 4: Finance and Resources
- Section 5: Development and Growth

3. Resident Services

Overview

This section covers issues raised in relation to:

- Manvers Street (Sneinton) Car Park
- Public Realm (including Pest Control)
- CCTV
- Community Protection (Antisocial Behaviour)

Manvers Street (Sneinton) Car Park

We were originally informed that this issue related to Sneinton car park but have now been told it relates to Manvers Street car park which is adjacent to a block of flats and is on HRA land.

Up to and including the financial year 2008/09 the HRA received the income from this car park. In 2008/09 the income received was £21,880. Our understanding is that since then the income has been retained in the GF. We are told that when the HRA tried to reclaim this income in 2017-18, the response was that the income was now part of the GF budgets and would not be paid to the HRA. Current Parking Services staff inherited the current arrangement.

In the period 2014-15 to 2020-21, actual income in relation to Manvers Street car park has totalled £159,058.20 (an average of £22,722.60). We do not have data relating to income in the five year period 2009-10 to 2013-14 or for 2021-22.

It appears that the cessation of payment of income from the Manvers Street car park in 2009/10 was an “administrative” oversight that has continued, even when it was brought to attention in 2017-18.

There is, understandably, no reference to car parks in the 2020 guidance since the operation of a public car park is not an HRA function. However, Circular 8/95 does refer to garages (and garage sites) let to non-housing revenue account tenants and states:

“Where an authority has a policy of letting, on a long-term basis, blocks of housing revenue account garages to people who are not housing revenue account tenants, the authority should consider appropriating the garages from Part II of the 1985 Act and accounting for them in the General Fund. The Department considers that, where tenants do not have the opportunity to rent the garages in a block, the provision of those garages does not form part of an authority’s housing function.”

Applying this principle, it seems that appropriation of the Manvers Street car park is the appropriate action to take going forward. However, until that is done, given the car park remains an HRA asset, it also seems appropriate that income from the car park is paid to the HRA, including any sums not paid in the past.

For the years for which data has been provided (including 2008-09), the average is £22,617.27. Applying this average for the years for which we do not have data, including the financial year just ended, the total income lost to the HRA is approximately £295,000. However, to confirm this figure, data for the missing years (2009-10 to 2013-14) will need to be obtained and income in 2021-22 identified.

Public Realm

Public Realm is responsible for a significant proportion of the charges made to the HRA by the GF. We have received data from both HRA Finance and GF Finance in relation to Public Realm Charges which do not reconcile. These are set out below (provided by HRA Finance):

	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21
Tree/horticultural Services	516,160	520,550	527,600	527,600	527,600	527,600	537,465
Grounds Maintenance	1,900,640	1,900,000	1,900,700	1,900,000	1,900,000	2,200,000	2,241,829
Street Lighting	279,960	282,340	285,020	285,020	285,020	285,020	285,020
Pest Control	-	-	-	-	-	-	40,000
Total	**2,696,760**	**2,702,890**	**2,713,320**	**2,712,620**	**2,712,620**	**3,012,620**	**3,104,314**

A number of issues were raised with us in relation to the above charges:

- In the past, the HRA received a substantial rebate, we are given to understand to reflect the number of RTB properties on Council (HRA) estates, but this was reduced in 2016/17 and disappeared completely in 2017/18
- The charge to the HRA was increased by £300,000 in 2019/20 for “Enhanced Grounds Maintenance” but no additional service has been provided
- A charge was introduced in 2020-21 to the HRA in respect of service recipients of Pest Control who are HRA tenants. In 2020/21 this amounted to £40,000.

In the course of our work, another issue in relation to Public Realm charges became apparent, namely the charge in relation to Street Lighting.

Rebate

In relation to the Rebate that was reduced and then disappeared, we have been provided with evidence by GF Finance of decisions taken to reduce and then eliminate this Rebate taken in Executive Board meetings to consider the MTFP.

- In relation to the MTFP 2016/17 to 2019/20 a recurring GF saving of £500,000 from 2016/17 is described as "Review of options and Housing Revenue Account considerations"
- In the MTFP 2017/18 to 2020/21 a recurring GF saving of £460,000 from 2017/18 is described as "Change in charges to Housing Revenue Account for shared services"

Despite effort to locate further evidence to explain and support the decisions made by the Executive Board, no further evidence has been found. In addition, evidence of how the Rebate was calculated has not been found.

Data provided by HRA Finance indicates the actual Rebate was:

- 2014-15: £935,300
- 2015-16: £943,250
- 2016-17: £454,410

These figures reflect the decisions taken by the Executive Board and also indicate that between 2014-15 and 2015-16 the Rebate increased, suggesting there was a basis on which it was calculated.

It seems reasonable that such a Rebate, to reflect RTB sales, should exist. Consequently it is hard to justify the reduction and subsequent elimination of the Rebate.

To the end of 2021-22, the lost Rebate amounts to £5,272,050. However, it should be noted that the Rebate if it has been in continuous payment may well have increased over time should it have been based on RTB sales which, it is assumed, have increased since 2015-16.

Increase in Grounds Maintenance Charge

The table above demonstrates the annual increase of £300,000 in 2019/20. It has been suggested to us that this increase was to reflect increased costs rather than the provision of an "enhanced service".

We have had sight of a draft SLA which indicates a proposed charge in 2022/23 of £2,727,600 (£2,200,000 for Streetscene and £527,600 for Parks and Open Spaces). This equates to the charges made in 2019-20 though is less than the charge in 2020-21.

This SLA is between NCC and NCH and, we are told, is under review. However, the SLA does not give any breakdown of the costs of specific activities or how the proposed costs are arrived at.

We have been told the cost of the services is not part of the SLA review but it is acknowledged that a wholesale review of the assets and the specifications for their maintenance needs to be carried out. This has been identified as a project, although not yet incepted. This work needs to be finalised so there is a clear and justifiable basis for the sum charged to the HRA.

Pest Control

We understand this GF funded service does not charge certain service recipients (e.g. if on benefits) but, since 2020/21, a charge is made to the HRA in respect of service recipients or are HRA tenants. In 2020/21 this amounted to £40,000. We understand those responsible for the HRA were not consulted on or involved in this decision but, instead, presented with a fait accompli.

The evidence we have been provided for this states that “The majority of NCH tenants would be in receipt of Council tax benefit and would therefore qualify for free pest control treatment, rather than being charged by the Pest Control service. In addition, any aborted visits (pest operative attends but cannot gain access to the residence) result in operational costs which currently have to be absorbed by the Pest Control service. This charge of £40k is to cover the costs of the tenants who receive a service free of charge”. The evidence provided also states the proposed charge in 2021-22 and in 2022-23 will be £40,000.

The fact it is a flat charge suggests it is not directly related to the number of HRA tenants who might qualify for free pest control treatment. The basis of how the sum of £40,000 was arrived at has not been evidenced.

In any case, in our opinion, given this is a GF service and it is Council policy to provide the service free of charge to people receiving benefits, it does not seem appropriate to differentiate between the people who are eligible for free pest control treatment based on the basis of their tenancy/ownership. The value of the charge to the HRA in 2020-21 and 2021-22 totals £80,000.

Street Lighting

As mentioned above, this issue came to light in the course of our work. The 2020 guidance includes Street Lighting in Non-Core Services. The guidance states “It is the view of MHCLG that it is inappropriate to assume that these services will be wholly charged to the HRA. Their costs should be met from the General Fund”

The total amount charged to the HRA between 2014-15 and 2020-21 is £1,987,400. Assuming the charge in 2021-22 remained the same as it has since 2016-17 (£285,020) the total amount at the end of 2021-22 would be £2,272,420.

CCTV

There is an historic charge to the HRA in respect of CCTV. Between 2014-15 and 2019-20 the annual charge was £1,358,000. In 2020-21 this increased to £1,380,848 and in 2021-22 it increased to £1,459,713.

The issue raised with us is that the basis of the charge is unclear and that there is no SLA in place. Given the amount of the charge remained unchanged for six years, it would suggest there was no real basis for calculating the charge other than, perhaps some historic basis. It has, however, increased in the last two years.

We have been provided with some details of a proposed SLA (with NCH) dated August 2020 by the GF Finance Business Partner but this could not be reconciled back to the charges made and was unsure whether this was the final version.

CCTV is recognised as a Core Service in the 2020 guidance. However, as with all charges to the HRA there should be a clear and justifiable basis for the sum charged to the HRA. Clearly, some work has been done to regularise the basis and sum charged to the HRA in relation to CCTV. This needs to be finalised.

Community Protection (Antisocial Behaviour)

There is an historic charge to the HRA. In 2014-15 this was £267,768. Between 2015-16 and 2019-20 the annual charge was £261,890. In 2020-21 and 2021-22 the annual charge increased to £287,890.

The issue raised with us is that the basis of the charge is unclear and that there is no SLA in place. Similar to the charge in relation to CCTV (above), the amount of the charge remained unchanged for some years (five years) but has increased in the last two years.

We have been provided with some details of a proposed SLA (with NCH) dated August 2020 by the GF Finance Business Partner but this could not be reconciled back to the charges made and was unsure whether this was the final version.

We have been provided with some details of a draft/unsigned SLA (with NCH) which does refer to the sum of £287,890 in 2020-21. However, the details provided to us do not set out how this sum is arrived at.

Antisocial behaviour is recognised as a Core Plus service in the 2020 guidance which states "Where the service is entirely charged to the General Fund it may be appropriate for the HRA to contribute to these costs".

However, as with CCTV, there should be a clear and justifiable basis for the sum charged to the HRA. Clearly, some work has been done to regularise the basis and sum charged to the HRA in relation to the Community Protection charge. This needs to be finalised.

4. Finance and Resources

Overview

This section covers issues raised in relation to:

- Solar (PV) Panels
- Corporate and Democratic Core
- Welfare Rights
- Support Services
- Debt Charges on Arboretum Properties

Solar (PV) Panels

Solar (PV) Panels are located on HRA properties. We understand that investment in Solar (PV) Panels was undertaken in two phases. The Senior Accountant (Capital Programmes) has provided us with information in relation to this investment, which is set out below:

- Investment in the first phase was in the period 2011-12 to 2013-14 and amounted to £8.542m. The 2011-12 and 2012-13 spend (£8.578m) was funded by HRA supported borrowing. It is assumed the 2013/14 spend (£0.004m) was funded by revenue contribution
- Investment in the second phase took place in 2015-16 to 2016-17 and amounted to £3.398m. As projects were not funded on a scheme by scheme basis during that period and as no grant was available it is assumed that this phase was funded by HRA Capital Receipts.

The HRA has received income since 2012-13 (presumably in relation to the first phase of investment). This amounts to a total of £12.967m up to and including 2021-22.

In addition, we understand the GF makes an annual payment of £0.216m over 20 years (totalling £4.320m) to the HRA due to the HRA funding the project. In this regard, the GF carries the risk/reward and receives the FIT income (net of repayment to HRA.) We have not been provided with details of the income received by the GF.

The particular issue raised in relation to Solar (PV) Panels is a contribution from the HRA to the GF based, we are told, on improving collection rates of FiT. However, we are also told that NCH has not delivered improved levels of collection so, the opinion expressed to us (when the issue was raised) is that this contribution is hard to justify. This contribution (from the HRA to the GF) was introduced in 2020-21 and amounted to £200,000. The same amount was budgeted for 2021-22 bringing the total to the end of 2021-22 to £400,000.

Given the streams of income from the first and second phases are delineated between the HRA (first phase) and the GF (second phase) and that the HRA is recompensed for the HRA investment in the second phase (though the annual payment made by the GF to the HRA) it seems hard to justify any additional contribution from the HRA to the GF. Even if such a contribution could be justified, it appears to us, it could not be a set amount if it is related to improved levels of collection.

Consequently, in our opinion, there is a case for recompensing the HRA for contributions in 2020-21 and 2021-22 which (if the budgeted amount on 2021-22 has been made) amounts to £400,000.

Corporate and Democratic Core

A charge in respect of Corporate and Democratic Core (Cost Centre 8900 - Corporate Management) to the HRA of £500,000 was introduced in 2019-20. The same charge was paid in 2020-21 and was budgeted for 2021-22.

We have not been provided with any evidence in relation to the basis of this charge or the reason for its introduction in 2019-20. Whilst, it may be considered acceptable for the HRA to bear a fair charge in relation to Corporate and Democratic Core (Corporate Management) it is essential that the amount and basis of such a charge to the HRA can be properly justified.

In the absence of such justification of the amount charged to the HRA, we are not in a position to comment on the fairness of this charge.

Welfare Rights

There is an historic charge to the HRA in respect of Welfare Rights. This charge has been in the sum of £283,200 since 2016-17 (in 2014-15 it was £282,762 and in 2015-16 it was £280,530) and was budgeted to be £283,200 in 2021-22.

The issue raised with us is that the basis of the charge is unclear and that there is no SLA in place. We have not been provided with any evidence in relation to the basis of this charge or the nature of the services provided to the HRA. However, given the amount the charge has remained unchanged since 2016-17, this would suggest there is no real basis (at least not currently) on which this charge is calculated.

It is essential that the amount and basis of such a charge to the HRA can be properly justified. In the absence of such justification of the amount charged to the HRA, we are not in a position to comment on the fairness of this charge.

Support Services

There are historic charges to the HRA for Support Services. The issue raised with us is that the basis of the charge is unclear and that there are no SLAs in place. The components of these charges and the annual sum since 2014/15 (provided by HRA Finance) are set out below:

Support Service Charges	Full Year Actual 2014-15	Full Year Actual 2015-16	Full Year Actual 2016-17	Full Year Actual 2017-18	Full Year Actual 2018-19	Full Year Actual 2019-20	Full Year Actual 2020-21	
Property Services-Ext	92,311	80,067	63,789	68,079	66,630	76,530	83,802	HRA Shops - time recharges
Recharge OT salary for Adaptations	16,685	17,548	18,112	17,575	17,083	18,853	20,040	1 post
Performance Management & Major Projects recharges	121,222	69,740	44,125	57,864	57,496	59,004	58,284	Variable - contribution to team cost
Property Services-Ext	51,767	40,617	53,283	0	0	0	0	Replaced by time charges
Finance Recharges	310,010	352,739	352,205	355,739	355,739	359,114	355,739	Includes Audit & Fraud in 19-20 (£3,375), not charged last year
EMSS Recharges External	73,360	11,753	11,735	11,853	11,853	11,853	11,853	
EMSS Recharges External	6,480	7,257	7,244	7,317	7,317	7,317	7,317	
IT Recharges External	143,200	152,582	154,950	154,950	154,950	156,500	130,760	Includes Switchboard recharge - missing in 20-21
Human Resources External	81,530	118,768	133,548	119,778	134,778	134,778	134,778	
Legal charges (Regen)	43,360	53,599	53,522	54,059	100,059	109,059	109,059	
Directorate Charge for time on HRA	23,380	23,380	23,610	23,380	23,380	23,380	23,380	
Finance Recharges	233,860	263,109	262,713	265,349	265,349	268,724	265,349	Includes Audit & Fraud in 19-20 (£3,375), not charged last year
EMSS Recharges External	0	8,767	8,749	8,837	8,837	8,837	8,837	
EMSS Recharges External	0	5,413	5,409	5,463	5,463	5,463	5,463	
IT Recharges External	108,030	114,008	111,640	111,640	111,640	114,008	93,400	Includes Switchboard recharge - missing in 20-21
Human Resources External	61,490	88,590	88,453	89,340	89,340	89,340	89,340	
Legal Services External	32,710	39,979	39,919	40,319	40,319	40,319	40,319	
Bank charges (from GF)	55,360	58,965	53,482	45,604	40,882	46,182	35,416	
Audit fees	3400	3400	0	0	0	0	0	Included in Finance Recharge
	1,458,155	**1,510,281**	**1,486,488**	**1,437,146**	**1,491,115**	**1,529,261**	**1,473,136**	

We have not been provided with any evidence in relation to the basis of these charges. As we have previously commented, it is essential that the amount and basis of such charges to the HRA can be properly justified. In the absence of such justification of the amounts charged to the HRA, we are not in a position to comment on the fairness of these charges.

Debt Charges on Arboretum Properties

HRA properties (in relation to the Arboretum) were sold to NCH but the capital receipt was transferred to the General Fund. This amounted to £1,608,500 in 2019/20 and was referred to in our Phase 1 report.

The issue raised with us is whether there was any debt outstanding on these former HRA properties and, consequently, whether the HRA is still being charged in relation to any outstanding debt on these properties.

We have been told by the Senior Accountant (Capital Programmes) that the properties in question at the Arboretum were historic housing stock and that there are, consequently, no associated debt charges borne by the HRA.

5. Development and Growth

Housing Partnership Team

There was formerly a recharge from the HRA to the GF in recognition that the Housing Partnership Team also work on GF activities (i.e. the private rented sector).

In 2015-16 and 2016-17 this was £45,500. In 2017-18 it was £45,890. Since 2018-19, there has been no charge and to the end of 2021-22, this would represent a loss to the HRA of £183,560.

We are told that this was presented as a fait accompli and it is not known how it was calculated before it was removed. No further evidence for the cessation of this charge from the HRA to the GF has been provided.

It is recognised that the Housing Partnerships Team does undertake GF activities so the cessation of the charge from the HRA to the GF is difficult to justify. Moreover, it has been questioned whether the sum should be higher although this would also need to be evidenced.

The amount should be reviewed and updated to cover a realistic proportion of the cost of staff that work on GF activities and reinstated. Alternatively, if possible, the costs should be split into HRA and GF cost centres.

It has also been suggested that the same approach should also apply to the Regeneration Team, who work on housing regeneration projects (not just HRA housing). This should equally apply to any income generated by the Regeneration Team.

In 2021-22 the net budget and FTEs associated with these teams was:

	Net budget 21/22	FTE
Regeneration	£1.979m	13.3
Housing Partnerships	£0.998m	8

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6. Conclusions and Recommendations

Overall Conclusions

We have considered the issues raised with us during the course of our Phase 1 work in this report. In Section 1 we comment on the difficulties encountered in finding evidence to support decisions that have been taken by NCC that impact on the HRA.

It is also apparent that, historically, decisions that impact on the HRA have been taken by NCC without full consideration of the HRA ring-fence and have been presented as a fait accompli to those responsible for administering the HRA.

On the basis of the evidence that has been provided to us and conversations with NCC staff in relation to this evidence, we do conclude that a number of decisions have been taken that cannot be justified and appear to undermine the HRA ring-fence. In particular:

- Loss of income to the HRA on Manvers Street Car Park (£295,000)
- Cessation of Rebate in relation to RTB in relation to Public Realm Charges (£5,272,050)
- Introduction of a charge to the HRA in relation to Pest Control (£80,000)
- Charges in relation to Street Lighting (£2,272,420)
- Contribution from the HRA to the GF regarding Solar (PV) Panels (£400,000)
- Cessation of an HRA charge to the GF regarding the Housing Partnership Team (£183,560).

In total, the above items amount to £8,503,030. However, it should be noted that these amounts are based on historic values which may well have changed since the relevant decisions were taken.

In addition to the above there are other issues that we have examined where a firm conclusion cannot be made on the fairness of the charges made to the HRA since there is no clear basis or SLA on which these charges are based. In particular we would draw attention to the £500,000 charge that was introduced in 2019-20 for Corporate and Democratic Core. No evidence has been provided to support this new charge.

There has been some work on developing SLAs undertaken (with NCH) but they do not seem to have the level of detail necessary to be a sound basis for calculating charges to the HRA and have not been finalised.

As we have commented a number of times in this report, it is essential that the amount and basis of all charges to the HRA can be properly justified in order to ensure the integrity of the HRA ring-fence.

Recommendations

We recommend that NCC considers our conclusions in relation to each of the items that combined have a value of £8,503,030 and determines:

- The amount the HRA should be reimbursed (taking into account any interest that might have accrued on the sums to be paid to the HRA)
- Any adjustments that might be necessary to reflect these amounts are based on historic values which may well have changed since the relevant decisions were taken.
- The actions needed to rectify these items from 2022-23 onwards.

We also recommend that work should be undertaken in relation to all charges to the HRA from the GF to provide a sound basis for the calculation of such charges combined with SLAs that have sufficient granularity to support these charges and any changes over time.

Finally, we recommend it should be mandatory that appropriate NCC staff with sufficient knowledge of the HRA ring-fence should be consulted before any decision impacting on the HRA is taken; ideally there should be an HRA “champion” who would need to agree to such decisions once satisfied such decisions do not breach the HRA ring-fence.

Annex A: Guidance – Operation of the Housing Revenue Account ring-fence

Published: 10 November 2020). Source: www.gov.uk

1. Introduction

This guidance updates and replaces Circular 8/95 published by the former Department of the Environment (DoE), to which the Ministry of Housing, Communities and Local Government (MHCLG) is a successor. It gives advice to local housing authorities in England on certain aspects of the Housing Revenue Account ("the HRA").

DoE Circular 8/95 provided valuable advice and gave clarification of whether various items of expenditure and income should be accounted for inside or outside the HRA. However, circumstances have changed: estates are not necessarily purely council-owned and an increasing proportion of those living on these estates are no longer tenants of the council.

This guidance restates ministers' established policy for the HRA and introduces no new issues of principle. However, it does highlight the need to be fair to both tenants and council taxpayers and that there should be a fair and transparent apportionment of costs between the HRA and General Fund.

This guidance is intended to be a helpful reference document for authorities, tenants and auditors. This guidance is not intended as an authoritative statement of the law on the keeping of the HRA, and authorities should take their own legal and accounting advice, as necessary, and will need to satisfy their auditors about their decisions.

2. Statutory background

Expenditure and income relating to property listed in section 74 of the Local Government and Housing Act 1989 ("the 1989 Act") must be accounted for in the HRA. This comprises mostly housing and other property provided by authorities under Part II of the Housing Act 1985 ("the 1985 Act").

Schedule 4 to the 1989 Act (as amended by section 127 of the Leasehold Reform, Housing and Urban Development Act 1993) specifies the debit and credit items to be recorded in the HRA. The Housing (Welfare Services) Order 1994 specifies the welfare services which must be accounted for outside the HRA.

3. General principles

The statutory provisions referred to above reflect the government's policy that the HRA remains a ring-fenced account within the General Fund; it should still be primarily a landlord account containing the income and expenditure arising from a housing authority's landlord functions.

Property in the HRA

At its most basic, when taking any decision on whether expenditure or income should be accounted for in the HRA, the test that should be applied is "Who benefits?" That is to say: who is the major contributor of the item of income, or the major beneficiary of the expenditure under consideration? Hence, should the HRA bear the full cost or only part, or should it benefit from the entirety of the income, or is some of it applicable to the General Fund?

In some cases, such as rental income or expenditure on housing repairs, it is clear that the HRA is the correct accounting vehicle. Conversely, legislation places transactions concerning rent rebates and housing benefits in the general fund. Nevertheless, there is a substantial 'grey area' of items of income and expenditure where differing and perhaps unique local circumstances will suggest different solutions. These are the decisions where local flexibility is best employed using the "who benefits?" approach.

The main consideration when deciding whether the costs and income associated with a particular property should be accounted for in the HRA is the powers under which the authority is currently providing that property. Section 74 of the 1989 Act sets out the property that must be accounted for in the HRA, by reference to the powers under which that property is held.

A property has to be accounted for within the HRA if it is currently provided under Part II of the 1985 Act or any of the other powers specified in section 74 of the 1989 Act (referred to here as "Part II housing"). The account also extends to any outstanding debts or receipts which arose when a property was so provided and which are still outstanding following its disposal.

If a property is not provided under the powers listed in section 74(1), or covered by a direction under section 74(1)(f), the authority must not account for it in the HRA - subject to certain exceptions set out in section 74(3). The HRA (Exclusion of Leases) Direction 1997, made under section 74(3)(d) of the 1989 Act, excludes from the HRA leases of up to 10 years for dwellings taken out by authorities for the purpose of housing homeless households.

If an authority wishes to include in the HRA property which is ancillary to Part II housing but not up to now provided under Part II, it will be necessary to obtain consent from the Secretary of State under section 12 of the 1985 Act (see also section 15 of the 1985 Act for London authorities). Such applications will be considered on their individual merits.

Equally, properties which may originally have been provided under one of the powers in section 74 of the 1989 Act (or their predecessor powers) may no longer fulfil their original purpose. In these circumstances, the authority should consider their removal from the HRA by appropriating the property to a different purpose. Examples of properties which might fall into this category are estate shops and other commercial premises, such as banks, post offices, workshops, public houses, industrial estates and surgeries, where there is no longer any connection with the local authority's housing.

The decision is for the authority to take, though it should be able to explain the basis of its decision to its external auditor and tenants, if called upon to do so.

Authorities should have regard to the powers available to them to hold property when they are considering whether to appropriate it out of the HRA. Section 19(2) of the 1985 Act requires authorities to obtain the Secretary of State's consent before a house, or part of a house can be appropriated for any other purpose.

If a property is transferred between the HRA and any other revenue account within the General Fund, this will involve adjustments to the HRA and other revenue accounts in accordance with any direction under paragraph 5(1) of part 3 of Schedule 4 to the 1989 Act and HRA capital financing requirements, and in accordance with the relevant determinations under Chapter 3 of Part 7 of the Localism Act 2011.

Amenities

These include play and other recreational areas, grassed areas and gardens and community centres. In each case it is for the authority to form its own judgement on whether provision is proper under Part II of the 1985 Act and the extent to which the costs should be charged to the HRA. There can only be a charge to the HRA where the amenities are provided and maintained in connection with Part II housing accommodation.

Where an amenity is shared by the community as a whole, the authority must have regard to paragraph 3 of Part III of Schedule 4 to the 1989 Act. This requires a contribution to be made from the General Fund to the HRA reflecting the general community's share of the amenity.

Management and maintenance services

The landlord is often best placed to provide wider services for neighbourhoods and communities that go beyond their traditional remit. When taking decisions locally, authorities need to demonstrate transparency to both tenants and Council Taxpayers that there is a fair apportionment of costs between the HRA and the General Fund.

To assist in determining what should and what should not be charged to the HRA, management and maintenance services can be expressed as core, core plus or non-core services.

Core services may be regarded as the 'bricks and mortar' functions of housing management, maintenance, major repairs and any associated debts and so forth. They are generally provided for the principal benefit of the landlord's tenants and leaseholders, not the wider community. Core plus services are those provided as additional services ancillary to the primary purpose of housing provision, which may have wider benefits to the overall community. A service that cannot be defined as core or core-plus should be accounted for in the council's General Fund.

Core services

- Repair and maintenance
    - Responsive
    - Planned and cyclical
    - Rechargeable repairs
- General tenancy management
    - Rent collection and arrears recovery
    - Service charge collection and recovery
    - Void and re-let management
    - Lettings and allocations of HRA properties only, any work carried out in respect of non HRA properties should be charged to the General Fund
    - Management of repairs
    - Antisocial behaviour: low level
    - General advice on tenancy matters
- General estate management
    - Communal cleaning
    - Communal heating and lighting
    - Grounds maintenance
    - Community centres
    - Play areas

    - Estate officers and caretakers
    - Neighbourhood wardens
    - Concierge
    - CCTV
- Policy and management
    - HRA share of strategic management costs
    - Setting of rent levels, service charges, and supporting people charges
    - Administration of the Right to Buy

Core plus services

- Contribution to corporate antisocial behaviour services. Where the service is entirely charged to the General Fund it may be appropriate for the HRA to contribute to these costs
- Tenancy support
- Maintenance of tenant gardens - unless a separate charge is made for the service
- Supporting people services - HRA housing related support services only, for example:
    - Sheltered accommodation wardens
    - Alarm services

Non-core services

It is the view of MHCLG that it is inappropriate to assume that these services will be wholly charged to the HRA. Their costs should be met from the General Fund.

- Administration of a common housing register – costs should be split appropriately between the HRA and General Fund
- Street lighting
- Dog wardens
- Personal care services
- Homeless administration
- Housing advisory service

The landlord should decide, within the requirements of existing legislation, whether it is appropriate to account for a proportion of these in the HRA or in the General Fund, using the 'Who benefits' principle. If the benefits of the service accrue primarily to the wider community, it is probable that the cost is a better fit in the General Fund, though it would be permissible to recoup a portion of any such cost from the HRA where it can be demonstrated that there is a benefit to HRA tenants or properties.

This does not imply any general discretion to transfer resources across the ring-fence; rather it is for the authority to apportion any costs or income for a service appropriately between accounts to reflect the benefit enjoyed by HRA tenants and leaseholders on one hand and the wider council taxpayer on the other.

Where a local authority is taking decisions concerning the correct place to account for new services or is reviewing existing practice in the light of evolving circumstances, the government would expect that tenants should be consulted, or involved in the decision-making process.

Homelessness administration

Authorities should consult the decision of the Court of Appeal in R. v London Borough of Ealing, ex parte Lewis, (1992) 24 HLR 484, when deciding how to account for homelessness administration costs. The case decided that not all the costs associated with homelessness administration by Ealing Borough Council should be charged to the HRA; only costs that fall within the description of 'management of houses and other property' can be included in the HRA.

Housing advisory services

The Court of Appeal's decision referenced above also covered Ealing Borough Council's costs on housing advisory services. Authorities should have regard to this aspect of the decision when considering the apportionment of costs relating to the provision of housing advice.

Part B: Workstream B Report

7. Introduction

Background

The focus of CIPFA's HRA Review (Phase 1) on behalf of Nottingham City Council (NCC) was the nature of the payments made by Nottingham City Homes (NCH) to NCC since 2014-15. NCC is dealing with the conclusions drawn in relation to this series of payments and the consequences for NCC and NCH.

In addition, however, the Phase 1 report identified the potential for further breaches of the HRA ring-fence:

Use of HRA funds to fund non-HRA activities

Concern has been raised during the course of our work about the possibility of HRA funds (or resources paid for by the HRA) being utilised by NCH on non-HRA activities.

Given that NCH needed to undertake a one-off exercise to support our current work in order to identify surpluses derived from HRA and non-HRA activities, it could be implied that there may be insufficient segregation and analysis of source of funds, application of funds and any resulting surplus or loss resulting from HRA and non-HRA activities undertaken by NCH.

The position is made more complex by inter-group transaction relating to services provided by NCH to its subsidiaries.

There is thus the likelihood that HRA funds provided to NCH are applied to non-HRA activities. This could potentially lead to breaches to the integrity of the HRA ring-fence.

There has been insufficient scrutiny of how HRA funds provided to NCH to ensure that HRA monies are spent on HRA related activities. This is exacerbated by the weakening of the HRA client function in NCC as a result of restructuring in 2016 together with the growth in NCH of non-HRA activities since the establishment of NCHEL and NCHRP in 2015.

It is also clear, from discussions held with NCH, that NCH does not consider that there is any obligation for it to account separately for HRA funds provided to it in relation to the services it provides to HRA tenants on behalf of NCC.

The focus of our work in Phase 2 (Workstream B) was, therefore, to identify the extent to which HRA monies were spent on HRA activities by NCH. Such analysis has been dependent on the sufficiency and adequacy of NCH's accounting records in allowing us to analyse the source and application of HRA (and non-HRA) funds.

This report sets out:

- Part 3: HRA funding and expenditure by NCH between 2014-15 and 2020-21
- Part 4: The steps required to regularise the ring-fencing of HRA funding in future

Acknowledgement

We are grateful for the constructive manner in which staff in NCH and NCC have provided information and responded to our queries.

8. HRA funding and expenditure by NCH between 2014-15 and 2020-21

As NCH does not consider that it has any obligation to ring-fence HRA funds, there is no statement available to show how such monies received have been applied each year. In the circumstances, therefore, we have focused on the income and expenditure in the consolidated financial statements for NCH each year in order to establish how HRA funds have been utilised. This section outlines:

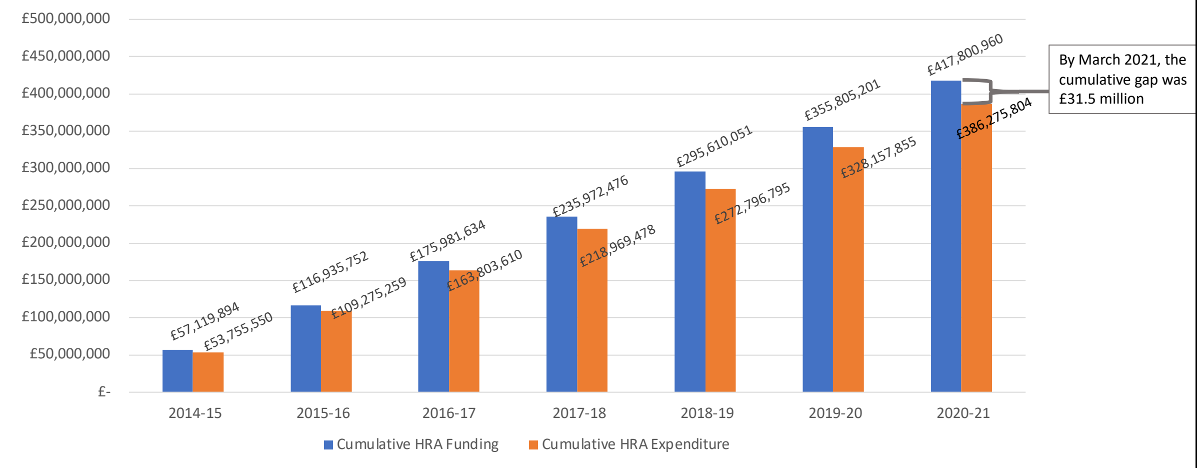
- The extent of the gap in HRA funding and expenditure between 2014-15 and 2020-21
- Our approach to quantifying the gap

The extent of the gap in HRA funding and expenditure between 2014-15 and 2020-21

The funding from the ring-fenced HRA account received by Nottingham City Homes Ltd and its subsidiaries between 2014-15 and 2020-21 exceeded its spending on HRA activities. As **Figure 1** below demonstrates, cumulative funding reached £417,800,960 by the end of 2020-21, whereas cumulative expenditure was £386,275,804. As a consequence, funding has exceeded expenditure by £31,525,117.

The gap grew the most between 2014-15 and 2018-19. HRA funding exceeded expenditure in 2014-15 by £3,364,344 and for the subsequent four years, funding increased by 4 per cent whereas expenditure remained the same. The difference closed somewhat between 2019-20 and 2020-21 when funding increased by 4 per cent, whereas expenditure rose by 8 per cent. This was mainly due to the construction of new council houses at Tunstall Drive and significant capital works in response to the Grenfell Tower tragedy to improve sprinkler systems and intercom speakers etc.

Figure 1: Cumulative HRA funding and expenditure between 2014-15 and 2020-21



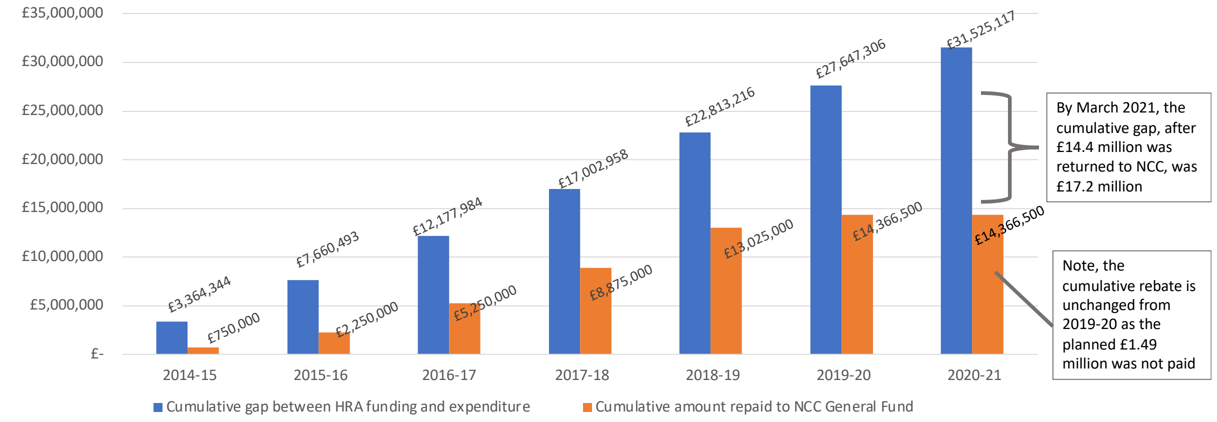
Source: CIPFA analysis of NCH data

The scale of the gap shown in Figure 1 does not take into account the annual payments made by NCH to NCC. Our previous report confirmed that such payments, after in-year adjustments, amounted to £14,366,500 between 2014-15 and 2019-20. The payments made by NCH to NCC were paid into the General Fund to help ameliorate the financial pressures facing the City Council. A further £1,492,000 was expected to be paid in 2020-21, but this transaction was halted.

We understand that NCC is already taking action to return the cumulative annual payments of £14,366,500 to the HRA. It is important, therefore, that these amounts are excluded from the calculation. As a consequence, **Figure 2** shows the scale of the remaining difference once these annual payments are removed.

On the assumption that the £14,366,500 is returned to the HRA, there remains a difference of £17,158,617 between HRA funding and HRA expenditure from 2014-15 to 2020-21.

Figure 2: The cumulative excess of HRA funding over HRA expenditure between 2014-15 and 2020-21 compared to the annual payments made to NCC



Source: CIPFA analysis of NCH data

The capacity for NCH to remedy this gap without support from the Council is constrained. The consolidated accounts for 2020-21 show that NCH did have a cash balance of £15,673,588 on 31 March 2021. This was essentially due, however, to the net receipt of £22,759,590 in loans from NCC in 2020-21 for non-HRA projects, such as the development of market rented properties by NHCEL (project 26047) and the developments at Arkwright Walk (projects 26049 & 26050) and the Clifton Triangle (project 26051). NCH explained that these loans were to replenish cash balances previously utilised to forward fund non-HRA investments. As figure 2 shows that there was an excess of HRA funding over HRA expenditure each year between 2014-15 and 2020-21, it is highly likely that the non-HRA investments were funded using HRA monies and have subsequently been replenished through a non-HRA loan. As we noted in our previous report, however, funding the HRA from the General Fund and vice versa represents a breach of the HRA ring-fence and so requires a formal direction from the Department for Levelling Up, Homes and Communities.

Our approach to quantifying the gap

Our approach involved:

- Stage 1: Establishing the account codes underpinning the 2020-21 consolidated financial statements
- Stage 2: Assigning each account code as, HRA, non-HRA or mixed
- Stage 3: Determining the reasonableness of the HRA and non-HRA allocations for each cost code

- Stage 4: Applying the categorisation developed for 2020-21 to the financial years 2014-15 to 2019-20
- Stage 5: Establishing the extent of any impact on the ring-fenced HRA fund

The following sections explain the work done and the key issues that arose during our work.

Stage 1: Establishing the account codes underpinning the 2020-21 consolidated financial statements

Our initial work involved confirming that the group account trial balance for 2020-21 aligned with the financial statements, the basis of the recharges between NCH, NCHRP and NCHEL, and thus the financial relationship between NCC, NCH and its subsidiaries. Key issues arising are set out below.

A. **The consolidated financial statements for NCH are dependent on a series of spreadsheet adjustments made at year end that are not clearly explained.** The spreadsheet with the trial balance includes a number of additional inter-company adjustments, tax adjustments, accruals and reserves adjustments. There are also figures in the preparation of the accounts, such as the composition of creditors, that are derived elsewhere. Whilst the NCH Director of Corporate Resources has been helpful in clarifying such queries, the absence of clearly explained working papers and robust supporting evidence together with the over-reliance on one individual to explain the transactions, risks, and potential delays in the preparation of financial statements in future.

B. **There is no ring-fencing of the management fee and repairs maintenance fee from the HRA.** Both funds are booked to a single account code (6005) and there are no other transactions against this account code[1]. In practice, this means that they are used as the 'de facto balancing item' on other cost codes. For example, the difference between the spend of nearly £684,000 on commercial repairs (code 5969) and associated non-HRA funding of nearly £472,000 in 2020-21 is likely to be effectively met from code 6005. There are 21 account codes that follow this pattern, with a net difference of £303,995 likely to be met from HRA funds. Similarly, there are also financial accounting codes used by NCH in 2020-21 that do not ring-fence HRA funding from non-HRA funding. The code 2800 for the Lettings Team, for example, includes nearly £453,000 NCC HRA funding, as well as £109,000 non-HRA funding from elsewhere. There are 10 account codes that include both HRA and non-HRA

[1] In comparison, capital fees and works are assigned to specific cost centres.

funding sources, with collective HRA funding of £2,135,075 and non-HRA funding of £639,464.

C. **There is insufficient differentiation between the accounting records for NCH and its two subsidiaries.** NCHEL has been assigned its own accounting code on the ledger (code 6009) and NCHRP the accounting codes 7000 to 7050. These codes are used to compile each company's accounts, but they do not enable differentiation between types of expenditure. For example, the costs incurred for relying on NCH staff and other resources are collated and booked to the inter-company subjective 'sub-contractors'. As a consequence, the financial statements for NCHRP and NCHEL do not provide any breakdown of operating costs and we have found it difficult to validate the figures.

D. We have not been able to confirm that NCH records of the funding received from NCC in 2020-21 reconcile with NCC records. The difficulties in reconciling the figures are possibly due to a lack of staff availability/familiarity with records. Nevertheless, there should be clear and available working papers that confirm the sums.

Stage 2: Assigning each account code as HRA or non-HRA

Our work involved consultation with NCH staff in order to establish the nature of each function and applying the 'who benefits' test to the functions associated with each account code. All activities undertaken by the two subsidiary companies, NCHEL and NCHRP, are non-HRA, but there are also other non-HRA activities undertaken by NCH.

We assigned 54 cost centres in 2020-21 as HRA – see Appendix 1. The list includes cost centres, such as repairs and maintenance where the activity covers both HRA and non-HRA work, but the non-HRA is removed through re-charges. We assigned 23 cost centres as non-HRA – see Appendix 1. These cost centres largely comprise commercial activities and the costs associated with properties owned by NCHRP and NCHEL.

The key issues arising are:

A. **We have challenged NCH's assessment that the cost of some programmes were associated with HRA funding.** The re-assignment of spending on 'Nottingham on Call' and the programme to improve energy efficiency as non-HRA is based on the principle that the schemes are not exclusive to Council tenants. These initiatives had combined expenditure of £2.6 million, with non-HRA funding of £1.7 million in 2020-21. We re-assigned all these costs as non-HRA accordingly.

B. **As it has not yet been feasible to separate the components of the ‘Central Charges’ cost code (6004) between HRA and non-HRA, costs were apportioned instead.** This cost centre comprises the costs incurred under the SLA with NCC for central services, such as IT and EMSS, as well as insurance costs and re-charges to NCHRP and NCHEL. We apportioned the expenditure between HRA and non-HRA based on property numbers managed by NCH (2,120 non-HRA out of a total of 27,513).

Stage 3: Determining the reasonableness of the HRA and non-HRA allocations for each cost code

NCH rely on inter-company recharges and the Northgate (NEC) housing management system to identify costs associated with the management of non-HRA properties. We examined how such costs are calculated and the journal entries required to extract non-HRA costs from otherwise HRA cost codes. The key issues arising were:

A. **NCC and NCH are determining the costs of maintenance and repair works and capital works based on a schedule of rates that cannot be validated.** The rates are bespoke to NCH and there is no record of how they were compiled. Without being able to substantiate the basis of each rate, it is not possible to confirm whether the costs incurred are reasonable. In the absence of such information, we have not amended the HRA and non-HRA allocations to reflect this issue.

B. **The Northgate system is highly likely to understate the costs associated with maintenance and capital works.** An exercise undertaken by the Director of Property Services found significant shortfalls when comparing actual costs incurred against the schedule of rates for a sample of works done. This is likely to arise as we understand that the schedule of rates has not been regularly updated since they were established around 2013. The extent of the shortfall is estimated to be at least 20%. The impact of this discrepancy is that charges to subsidiaries and non-HRA activities could be significantly understated, in effect providing an illegitimate HRA subsidy. We have, therefore, increased the non-HRA costs associated with such activities by 20%, thereby reducing the HRA spend.

C. **The cost of works done by the in-house Construction Repairs and Maintenance team does not include the cost of central overheads within NCH.** Our understanding is that the rates cover the materials and direct labour costs for the teams, as well as an element of overhead for the management team and administrative staff within the directorate. The rates do not, however, include the costs associated with the management team in NCH or central administrative functions, such as finance, HR, IT etc. Given the likely under-recovery of costs for work undertaken by the in-house Construction Repairs and Maintenance team, we have assigned an additional 20% of the recharges as non-HRA.

D. **Non-HRA costs are charged to NCH's subsidiaries, but the amounts are based on assumed costs per property rather than actual costs.** For example, the service level charge per 50 dispersed properties of £286,000 includes:

- Employee costs of £154,329 – based on an assumption of 3.8 Grade 5 staff at £33,115 and 0.6 Grade 8 staff at £45,650.
- Voids cleaning/other of £42,089 – based on the assumption of each of the 50 properties being cleaned twice a year at £400 each, plus an extra £2,089 for 'other' works.
- Repair costs of £39,000 – based on the assumed need to recommission gas and electrics for each of the 50 properties twice a year at £390 each time.
- Alarm/contact service of £24,811 based on the assumption of having to pay individual(s) £9.54 per week, per property.

There is also an overhead charge of £24,579, but we have not been able to establish the basis of this figure. In the absence of reliable data, we have not revised the HRA and non-HRA allocations to reflect this issue.

Stage 4: Applying the categorisation developed for 2020-21 to the financial years 2014-15 to 2019-20

Having determined the basis of the allocations for 2020-21, we applied the same principles to earlier years. The account codes are essentially the same each year – there were 21 codes in 2020-21 that did not exist in previous years, and 13 codes that existed in earlier years but not in 2020-21. The latter were either incorporated into other codes (such as 'Company Secretary' becoming part of 'Governance') or reflected specific HRA projects, such as the construction of council houses at Amber Hill and the installation of smoke alarms.

Key points to note are:

- **The extent of the understatement of costs by the Northgate system is likely to be lower in earlier years.** We had assumed a 20% understatement in 2020-21.

Accordingly, we assumed an understatement of 18% in 2019-20, 16% in 2018-19, decreasing by 2% each further year to 8% in 2014-15.

- **Where costs were apportioned on the basis of the number of HRA and non-HRA properties managed by NCH, we have revised the proportions to reflect the breakdown in earlier years.**

Stage 5: Establishing the extent of any impact on the ring-fenced HRA fund

In order to determine the extent of the gap between HRA funding and expenditure each year, we assigned each cost code against the headings used in the financial accounts and reconciled the totals to each set of audited financial statements.

Accordingly, the table below shows HRA funding and expenditure each year.

HRA Income & Expenditure	2014-15 (£)	2015-16 (£)	2016-17 (£)	2017-18 (£)	2018-19 (£)	2019-20 (£)	2020-21 (£)
Turnover							
NCC funding:							
□ Management fee	22,014,000	23,005,000	22,516,000	22,841,996	22,996,000	22,374,000	22,649,000
□ Repairs and maintenance	26,804,150	27,260,000	27,260,000	27,329,004	27,167,004	26,899,000	26,884,000
□ Capital fee	2,257,573	2,631,587	2,857,612	2,301,939	1,829,757	1,637,978	1,155,738
□ Capital works	5,779,211	6,694,921	6,174,041	7,212,739	7,322,902	8,328,748	10,449,612
□ NCC other	264,960	224,350	238,230	305,164	321,913	955,424	857,409
Total income	**57,119,894**	**59,815,858**	**59,045,882**	**59,990,842**	**59,637,575**	**60,195,150**	**61,995,759**
Expenditure	**53,755,550**	**55,519,709**	**54,528,351**	**55,165,868**	**53,776,543**	**55,328,423**	**58,103,803**
Interest payable/receivable	0	0	0	0	50,744	32,637	14,146
Operating Profit (Loss)	**3,364,344**	**4,296,149**	**4,517,491**	**4,824,974**	**5,810,258**	**4,834,090**	**3,877,811**

Similarly, the table below shows the commensurate non-HRA income and expenditure each year:

Non HRA Income & Expenditure	2014-15 (£)	2015-16 (£)	2016-17 (£)	2017-18 (£)	2018-19 (£)	2019-20 (£)	2020-21 (£)
Turnover							
NCC funding:							
Repairs and maintenance	61,014	263,638	731,382	1,376,093	1,706,909	1,540,453	444,999
Nottingham on call	613,033	561,012	715,696	920,770	944,478	831,829	818,120
NCC other	626,111	1,618,828	1,098,509	613,596	330,417	524,063	528,168
Other income sources:							
Rental income	17,085	215,774	467,158	1,045,231	2,608,073	3,974,626	5,938,808
Govt funding	0	0	253,322	124,016	144,054	562,415	710,305
Other	941,302	925,296	566,476	815,992	1,051,273	1,180,450	1,472,195
Total income	**2,258,545**	**3,584,548**	**3,832,543**	**4,895,699**	**6,785,204**	**8,613,835**	**9,912,596**
Expenditure	**4,074,624**	**4,371,874**	**4,285,553**	**5,372,187**	**6,294,136**	**8,017,265**	**8,677,890**
Interest payable/receivable	(15,476)	51,373	269,977	498,971	725,647	1,045,402	1,299,190
Operating Profit (Loss)	**(1,800,603)**	**(838,699)**	**(722,987)**	**(975,459)**	**(234,579)**	**(448,832)**	**(64,484)**

9. The steps required to regularise the ring-fencing of HRA funding in future

In our opinion, the duty of a Local Housing Authority (LHA) is to ensure that HRA monies are only spent to the benefit of HRA tenants (the “Who benefits?” test) does not cease when an LHA enters into arrangements for a service provider to provide services to tenants on its behalf. There remains a statutory responsibility on the LHA to ensure that HRA funds provided to the service provider (and consequently outside the day-to-day control of the LHA) are spent to the benefit of tenants. This applies to HRA monies provided by NCC to NCH.

It is also clear, from discussions held with NCH, that they consider that there is no obligation on them to account separately for HRA funds provided or to demonstrate that such monies are only utilised on the services it provides to HRA tenants on behalf of NCC.

Consequently, current reporting and accounting arrangements with NCH do not provide assurance to NCC (as the LHA) that HRA monies have been properly spent to the benefit of HRA tenants only; i.e. that the “Who benefits test?” extends to the provision of services provided to tenants by NCH on behalf of NCC. This will need to change in future.

More robust arrangements between NCC and NCH in relation to HRA monies (though they equally apply to GF monies provided to NCH) should be applied to protect the interests of HRA tenants. Our interim report identified three key areas:

- **Budgeting.** NCC needs to agree a budget for each element of HRA funding (Management Fee, Repairs Fee etc.) with NCH. In the past this appears to have been done on an incremental basis and at an insufficiently granular level of detail, with the potential of conflating HRA and non-HRA spending pressures on NCH. Ideally, this would be based on a zero-based budgeting exercise, though we recognise it is too late for this to happen in agreeing the 2022-23 budget. Such an exercise, however will allow NCC in dialogue with NCH, to properly cost the services provided to the HRA at an appropriately granular level of detail (e.g. which posts or proportion of a post are funded by the HRA in NCH). NCC should also consider what might be a reasonable level of surplus for NCH to earn from the services it provides to the HRA if this is considered appropriate.

- **Service Level Agreements (SLAs).** Budgets for the HRA funding provided to NCH should be set and agreed with NCH on the basis of granular SLAs (encompassing the Management Fee, Repairs Fee etc.) that sets out the purposes for which the funding is provided and the spending that the funded is intended to support (e.g. which posts or proportion of a post are funded by the HRA in NCH).
- **Reporting and Accounting.** NCC should require NCH to account for and report on HRA activities separately from non-HRA activities (encompassing both financial and non-financial reporting). This will enable NCC as the LHA to:
  - Have clarity on how HRA funds have been applied by NCH and determine whether HRA funds provided to NCH have been fully spent on HRA activities (excluding any reasonable surplus that has been agreed and built into the arrangements between NCC and NCH);
  - Determine, where HRA funding provided to NCH has not been fully spent on HRA activities, to what extent a legitimate rebate to the HRA is appropriate or, potentially, the sum be carried over to reduce the burden on the HRA in future years;
  - Have clarity on budgetary pressures experienced by NCH in relation to HRA activities in isolation (budgetary pressures in relation to services funded by the GF should be dealt with separately) and determine how these should be dealt with in subsequent budgets (e.g. though increased funding and/or savings/efficiencies within NCH);
  - Report on HRA spend on an "actuals" basis in the annual HRA financial statement (we understand HRA spend is currently reported on the basis of funds provided to NCH so effectively what is budgeted rather than what has been spent).

In relation to the intra-group company transactions within the NCH, NCC, as sole shareholder, should require that:

- Ensure that costs are properly charged between companies throughout the year based on actual costs. This should include all relevant overhead costs.
- Maintain balance sheet records for each company to include property assets for those properties under the control of the relevant subsidiary
- Provide monthly management accounts for NCC on each of its subsidiaries and present draft accounts for each entity to NCC both pre and post audit.

Following on from our interim report, we sought to separate the balance sheet between HRA and non-HRA activities. This proved problematic and highlighted a number of other issues that will also need to be addressed:

- **Fixed assets.** It should be relatively straight forward to differentiate HRA from non-HRA assets. Any land and buildings within the NCH consolidated accounts would constitute non-HRA assets. In practice, however, we were unable to reconcile the list of properties managed on behalf of NCC – the list held on the Northgate system (31 March 2021) refers to 25,328 properties, whereas the records supporting the financial statements for NCH refer to 25,393. There is a discrepancy of 65 properties that we have been unable to reconcile. It is not clear if the additional 65 properties are Council owned or NCH owned. There should be regular reconciliations to support the fixed asset registers held by the Council and NCH.
- **Working capital.** We have not been able to establish a satisfactory breakdown of debtors and creditors between HRA and non-HRA activities, and thus the cash flow impact on the closing cash balance. The working papers supporting the associated figures in the financial statements are difficult to follow, and the volumes of individual transactions that compile the figures mean it would be a considerable task to unpick the numbers with any accuracy. In the circumstances, any differentiation required between HRA and non-HRA for past years may be more cost effective if it were based on a retrospective apportionment based on the number of HRA and non-HRA properties instead.
- **Equity.** Whilst the separation of income and expenditure between HRA and non-HRA activities enables the impact on the profit and loss reserve to be determined, £45.8 million of the £49.9 million change in equity (92 per cent) from March 2020 to March 2021 was due to increases in the actuarial value of defined benefit pension obligations and in the fair value of pension fund assets held. Segregating the pension values of HRA funded staff from non-HRA funded staff for past years is difficult and, as with working capital, it may be more cost effective if it were based on a retrospective apportionment based on the number of HRA and non-HRA properties instead.

Annex 1: The allocation of cost centres in 2020-21 as HRA and non-HRA

Cost code	HRA	Non-HRA
Adaptations	x	
Apprentices	x	
Aspley Area Office	x	
Asst Director Housing Services	x	
Asst Director Tenancy & Estate	x	
Asset Planning & Strategy	x	
Assistant Director Asset Manag	x	
Beechdale Court	x	
Bestwood Area Office	x	
Building Expenses	x	
Building Safety Team	x	
Bulwell Area Office	x	
Business Intelligence	x	
Business Transformation	x	
Capital Grants Received in Adv	x	
Capital Programme Delivery	x	
Central Charges	x	
Central Charges RP		x
Chief Executive	x	
Clifton Area Office	x	
Commercial Team		x
Commercial Works - Arboretum 1		x
Commercial Works - Forest Road		x
Commercial Works - Harvey Road		x
Commercial Works - NCC Repairs		x
Communications & Marketing	x	

Cost code	HRA	Non-HRA
Communications Team	x	
Customer Experience	x	
Day to Day	x	
Decent Neighbourhoods	x	
Developments	x	
Director of Corporate Services	x	
Director of Housing	x	
Dispersed Tenancies		x
Dispersed Tenancies Acquisition		x
District Heating	x	
Door & Window Renewals	x	
Driveway Works	x	
Electrical Contract Costs	x	
Employment Provision		x
Energy - Communal		x
Energy Delivery		x
Estate Caretaker Service	x	
Estate Works	x	
Finance	x	
Fire Damaged Properties	x	
Fire Risk Response	x	
Fit for the Future		x
Gas, Smoke Alarm & H/Watch Ser	x	
Governance	x	
Grander Designs	x	
Head of Governance, Risk & Com	x	
Heating & Boiler Installations	x	
Heating Installations Phase 2	x	
Heating Repairs	x	

Cost code	HRA	Non-HRA
High Rise Living	x	
Highwood House		x
Hyson Green Area Office	x	
Independent Living Complexes	x	
Independent Living Mngt	x	
Internal Maintenance Works	x	
IT Expenses	x	
Kitchens & Bathrooms	x	
Landlord Services Stonebridge		x
Landlord Services Wainwright		x
Leaseholder & Rechargeable Rep	x	
Lettings Team	x	
Lift Maintenance	x	
Loxley Accommodation	x	
Major Electrical	x	
Major Works	x	
Management Fee Income	x	
Market Rented		x
Mechanical Contract Costs	x	
Move-On		x
NCH Owned Properties		x
NCH RP Dispersed Tenancies		x
NCH RP Dispersed Tenancies 2		x
NCH RP Highwood		x
NCH RP Private Sector Leases		x
NCH RP Social Housing		x
New Build - Wells Road	x	
Nottingham On Call		x
Organisational Development	x	

Cost code	HRA	Non-HRA
Out of Hours	x	
Painting	x	
Private Sector Leasing		x
Radius Cash Receipting Susp		
Rents Team	x	
Repairs & Maintenance AD	x	
Revenue Voids	x	
Risk Management	x	
Safer Neighbourhood Housing	x	
Sanctuary		x
Section 106 Agreements		x
Service Level Agreements	x	
Sprinkler Installations	x	
St Anns Area Office	x	
Stores	x	
Technical Services	x	
Tenant & Leaseholder Involvement	x	
Tenants Community Facilities	x	
Transport	x	
Tunstall Drive	x	
Vehicle Grant	x	
Victoria Centre Area Office	x	
Voids Cleansing	x	
Zedra		x