

Committee: Cabinet
Date: 16 February 2012
Title: Medium Term Financial Strategy
Portfolio Holder: Councillor Robert Chambers

Agenda Item

13iv

Item for
Decision

Summary

- 1 As part of the annual budget setting process, the Medium Term Financial Strategy (MTFS) is due to be considered by Full Council on 23 February.
- 2 The Scrutiny Committee reviewed the MTFS on 7 February and endorsed the contents.
- 3 The MTFS shows the following:
 - The extreme difficulty in making reliable forecasts about Government funding from 2013.
 - Anticipated progressive replacement of core Formula Grant funding with New Homes Bonus.
 - There is a material financial uncertainty relating to the replacement of Council Tax Benefit with a localised system of Council Tax Discounts.
 - The Council has made substantial progress towards its target of reducing annual running costs (and/or increasing income) by £2m per annum by 2014
 - Inflationary pressures and possible funding reductions mean that the Council needs to find additional savings and income of up to £0.9m per annum by 2016/17.
 - The Strategic Solutions Workstreams have sufficient projects underway or planned to achieve the level of savings.
 - Subject to the uncertainties highlighted, the Council will be able to maintain reserves at a prudent level during the MTFS period.

Recommendations

- 4 The Cabinet is requested to approve, for recommendation to Full Council, the Medium Term Financial Strategy as set out in this report.

Financial Implications

- 5 Detailed in the report.

Background Papers

MTFS approved by Full Council February 2011

MTFS update approved by Cabinet September 2011

Budget Strategy approved by Cabinet September 2011

Budget papers elsewhere on today's agenda

Impact

Communication/Consultation	None
Community Safety	None
Equalities	None
Health & Safety	None
Legal implications	It is a legal requirement to set a balanced budget
Sustainability	The MTFS is designed to ensure the financial stability and sustainability of the Council over the medium term
Ward-specific impacts	None
Workforce/Workplace	Some of the savings will have workforce implications

Medium Term Financial Strategy (MTFS)

- 6 The MTFS complements the Corporate Plan by setting out the anticipated resources available to enable the delivery of corporate priorities. It predicts the costs that will be incurred and estimates available income, and thus quantifies the level of saving necessary to balance the budget.
- 7 The MTFS covers the Corporate Plan period on a rolling five-year basis and thus this updated MTFS is for the period 2012/13 to 2016/17.
- 8 In keeping with the new 'one-page' format of the Corporate Plan, the MTFS is a briefer high level summary than its previous iterations. Its focus is the General Fund revenue budget, that is to say, budgets for all services except the provision of council housing. Council housing budgets are covered by the 30 year HRA business plan. Capital expenditure is also excluded as this is covered by the 5 year Capital Programme. The interactions between the HRA, Capital Programme and General Fund have been built into the MTFS projections.
- 9 In a formal sense the MTFS is approved by the Council annually as part of the budget setting process, and undergoes a formal mid-year review by the Cabinet. In between these half-yearly updates, officers monitor the financial situation and will bring issues to Members' attention as required.

Key assumptions used

- 10 Necessarily the 5 year forecast is based on assumptions about the future. Below are the key assumptions used. Members should be comfortable that the assumptions are reasonable, neither unduly optimistic or pessimistic.

Government Funding

- 11 Government funding has always had a degree of unpredictability about it, with Formula Grant levels not confirmed until the end of January prior to the financial year to which it relates, and funding under other schemes often not confirmed until just prior to the start of the year, after budgets are set. However, uncertainty about Government funding is currently at an unprecedented high level.
- 12 There no firm information available to estimate funding levels from 2013, and the Government is carrying out a root and branch review of local government funding such that basic tenets and principles no longer apply.
- 13 Core funding currently comes by way of **Formula Grant**, which is just under £2.8 million for 2012/13. There is no information about Formula Grant from 2013/14 onwards; there is a real possibility that it will be reduced, and in due course, phased out altogether.
- 14 In its place is likely to be a strong emphasis on rewarding councils whose localities have experienced housing growth and economic development. Councils will have a direct financial incentive to ensure such growth and development, equally, they could see their funding reduced if there is no such growth.
- 15 **New Homes Bonus** rewards local authorities for housing growth. It is a six year scheme, with 2012/13 being year two. In summary, councils receive a sum equivalent to the average English Council Tax bill, around £1,500, for each new dwelling (Band D equivalents). For example, if there are 333 new dwellings arising in the year, the council concerned would receive £500,000 in New Homes Bonus per year until the end of the scheme. This is compounded as illustrated in the table below.

UDC New Homes Bonus payments £000	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
	Actual	Actual	Estimate	Estimate	Estimate	Estimate
Housing growth year ending Oct 2010	714	714	714	714	714	714
Housing growth year ending Oct 2011		534	534	534	534	534
Housing growth year ending Oct 2012			500	500	500	500
Housing growth year ending Oct 2013				500	500	500
Housing growth year ending Oct 2014					500	500
Housing growth year ending Oct 2015						500
Total New Homes Bonus received	714	1,248	1,748	2,248	2,748	3,248

- 16 Despite the significant projected increases in New Homes Bonus funding, it is not realistic to expect the Council to realise the full benefit of these increases. The Government has not allocated sufficient funding to meet the commitments arising from the New Homes Bonus scheme, and has stated that any shortfalls will be met from Formula Grant from 2013/14. **The MTFS assumes that there will be reductions in Formula Grant from 2013/14, to pay for New Homes Bonus.**

- 17 The core assumption in the MTFS is that the base amount of total funding receivable by the Council from the two sources Formula Grant and New Homes Bonus, will be equivalent to the total level in 2012/13 i.e. there shall be no net increase in funding.
- 18 Furthermore, the MTFS needs to estimate what the Government may do in the 3rd and 4th years of the present Spending Review period, 2013/14 and 2014/15. Deficit reduction remains the key priority for the Government. In the first two years of the Spending Review period, the Council's Formula Grant was cut by 28%, one of the most severe reductions in the country. It is prudent to assume that further reductions will be made in the subsequent two years. **The MTFS assumes a reduction in the total of Formula Grant and New Homes Bonus of 10% per year for 2013/14 and 2014/15.**
- 19 The Council could be financially vulnerable in the event of low housing growth or Government reform of the scheme, or lack of continuation beyond 2016/17.
- 20 **Localisation of Business Rates** is another aspect of the Government's reforms that will see adjustments to Formula Grant from 2013/14 resulting from changes to the level of business rates income. At present all business rates collected are transferred to the Government. From 2013/14, councils will keep a share of any increase in business rates above a baseline level (to be determined), and similarly, will be required to make good any reductions in business rates below the baseline. This provides another direct financial incentive to councils to ensure economic growth.
- 21 The Government intends to operate a complex set of baseline adjustments, top-ups, tariffs, levies, thresholds and re-sets so that no individual council is unjustly enriched or penalised under the scheme. Exactly how this will operate is not yet clear and it is not possible to estimate the effect on UDC. At this stage therefore, **the MTFS assumes that the effect of business rates localisation will be neutral.**
- 22 It would be a prudent manoeuvre to establish some form of contingency reserve against fluctuations arising from business rates localisation. This has been factored in to the MTFS at a provisional £150,000 per year from 2013/14. There is a possibility of pooling arrangements with other councils being set up that will mitigate risk. When more information is available about such arrangements, an assessment can be made of the degree to which UDC should maintain its own contingency funds.
- 23 The effect of the assumptions above is to assume that the total Government funding, in whatever combination of Formula Grant and New Homes Bonus may arise, will reduce but not fall below the predicted level of New Homes Bonus for 2016/17, as shown in the summary table below.

£000	2012/13	2013/14	2014/15	2015/16	2016/17
Formula Grant	2,767				
New Homes Bonus	1,248				
Business rates adjustment		0	0	0	0
Total	4,015	3,614	3,253	3,253	3,253
		10% reduction	Further 10% reduction	No change	No change and in line with estimated total NHB as per table above

Council Tax and Council Tax Freeze Grant

24 In recent years the Government's policy has been to strongly encourage councils to minimise Council Tax increases.

25 Decisions about each annual increase will be taken in the February of each year according to the needs and circumstances arising at that time. Having taken informal guidance from the Finance Portfolio Holder, **the MTFS includes a planning assumption that the district council tax will be frozen in 2012/13, and will be increased by 2.5% per annum thereafter.**

26 **The MTFS also assumes an annual taxbase growth of 1%**, consistent with recent experience.

27 The table below shows projected Council Tax income over the MTFS period.

	2012/13	2013/14	2014/15	2015/16	2016/17
Council Tax Base (Band D equivalents)	33,732	34,069	34,410	34,754	35,102
District Council Tax (Band D)	£147.42	£151.11	£154.89	£158.76	£162.73
Increase on prior year	£0.00	£3.69	£3.78	£3.87	£3.97
Council Tax Income (£000)	4,973	5,148	5,330	5,518	5,712

28 In 2011/12, the Government introduced a new Council Tax Freeze Grant to compensate councils who froze their Council Tax. The grant was equivalent to the amount of income foregone assuming a 2.5% increase, and is payable for 4 years, with 2012/13 being year 2. In addition, a one off Council Tax Freeze Grant for 2012/13 has been announced, again equivalent to a 2.5% increase, but payable for one year only. **The MTFS assumes there will be no further awards of Council Tax Freeze Grant.**

£000	2012/13	2013/14	2014/15	2015/16	2016/17
Council Tax Freeze Grant 2011/12	123	123	123	0	0
Council Tax Freeze Grant 2012/13	125	0	0	0	0
Total	248	123	123	0	0

Reform of Council Tax Benefit

- 29 Council Tax Benefit (CTB) is currently a national scheme that councils run on the Government's behalf. The Government sets the rules on eligibility, and reimburses councils for the cost of CTB claims processed correctly.
- 30 From 2013/14, the Government intends to abolish CTB and require district councils to develop local schemes in the form of Council Tax discounts. The Government will fund the scheme, but with a 10% cut in funding compared with CTB. Whether the 10% cut will be per authority or the average is not yet clear. The funding will be cash limited i.e. any increase in demand will be funded by councils, not the Government.
- 31 Council Tax discount schemes will be required to protect "pensioners" and "vulnerable people" (neither term is defined) and be designed in such a way as to incentivise low-incomed people not in work and claiming benefit to start working. Clearly this could have serious policy and reputational implications and represents a major challenge for the Council in 2012; new schemes have to be published by January 2013, for implementation from April 2013.
- 32 In addition, the financial consequences could be profound; if the local scheme eligibility criteria are not robust, demand for the scheme could exceed expectations, with the costs borne by the council not the Government. (It is likely that cost sharing with other authorities would operate).
- 33 Another risk is the increased resources required to collect Council Tax from households currently in receipt of CTB but may not qualify for a discount or a local scheme.
- 34 Implementation costs will be a factor with IT system development and public consultation required during 2012. It is not yet clear that IT providers are able to deliver in line with the timetable the Government has set out.
- 35 Clearly this is a major financial uncertainty for the Council. The MTFS assumes that:
- Expenditure under the local Council Tax discount scheme will be the same as for CTB, adjusted for annual taxbase and Council Tax rises
 - Government funding will be cut by 10% from 2013/14
 - Implementation costs will be met from reserves, such as the Housing Benefits reserve. (Neither the costs nor use of reserves are included in the figures).

Use of New Homes Bonus (NHB)

- 36 The Cabinet decided to allocate £500,000 from the 2011/12 NHB funding of £714,000 for one off community projects. The 2012/13 budget includes proposals to earmark £708,000 from the £1,248,000 allocation. The MTFS assumes that from 2013/14, New Homes Bonus will progressively supplant core Formula Grant funding, as explained above. Therefore, the Council's capacity to continue to earmark NHB for one off spend will reduce, and increasingly, NHB will be required to fund the Council's base budget. The MTFS includes the following assumptions.

£000	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
Estimated New Homes Bonus award (as shown above)	714	1,248	1,748	2,248	2,748	3,248
Amount earmarked for community schemes & one off projects	500	708	500	300	100	0
Amount transferred to earmarked reserve	214	540	0	0	0	0
Amount used to fund Council budget	0	0	1,248	1,948	2,648	3,248

Inflation assumptions

- 37 At time of writing, inflation (December 2011 figures) is at 4.8% (RPI) and 4.2% (CPI), but is falling. Analysts predict that inflation will continue to fall during 2012/13. In addition, the Government's target is to reduce inflation to 2%. The cost of fuel and utilities remain volatile, however, and subject to larger cost increases than general price inflation.
- 38 The Government's pay policy for public sector employees is to cap increases at 1% per annum. For local government, national pay bargaining arrangements apply; there is no guarantee that Government pay policy will be applied. This is something that the Council has no control over.

MTFS assumptions	Approx value of each 1% change	2013/14	2014/15	2015/16	2016/17
Pay award	£80,000	1%	1%	2%	2%
Staff pay increments	£80,000	0.5%	0.5%	0.5%	0.5%
Supplies & services inflation (contractual indexation)	£28,000	3%	2.5%	2%	2%
Supplies & services inflation (other)	£26,000	2%	1.5%	1%	1%
Utilities & fuel	£6,000	10%	10%	10%	10%
Fees & charges income (except car parks)	£40,000	2%	2%	2%	2%
Car parks income	£8,500	0%	0%	0%	0%
Pension Fund Deficit contribution	£5,000	3%	3%	3%	3%
Housing Benefits (private)	£90,000	3%	2.5%	2%	2%
Housing Benefits (rent rebates)	£65,000	6%	5.5%	5%	5%
Council Tax Benefit (see above)	£40,000	3.5%	3.5%	3.5%	3.5%
DWP funding for benefits (see above)	£195,000	In proportion with total benefits spend; £400,000 reduction re. CTB	In proportion with total benefits spend	In proportion with total benefits spend	In proportion with total benefits spend

Other assumptions

- 39 Capital financing costs to increase by £100,000 per annum as the Council will become dependent upon external borrowing to finance the Capital Programme.
- 40 Recharge of costs & overheads to the HRA will remain constant.
- 41 Investment income will remain constant for first 3 years then start to increase from 2015/16 in line with interest rate forecasts.
- 42 The Collection Fund balance will be zero from 2013/14 onwards (currently £10,000 deficit).
- 43 The Working Balance will be maintained at a level equivalent to the sum of 2% of expenditure and 2% of income.

5 year financial model

- 44 Based upon the draft 2012/13 budget being presented for approval and the assumptions detailed above, a five-year forecast has been prepared and is summarised below.

£000	2012/13	2013/14	2014/15	2015/16	2016/17
Service Expenditure	33,464	34,470	35,525	36,672	37,700
Service Income	-25,428	-25,901	-26,769	-27,545	-28,350
Net Service Expenditure	8,036	8,569	8,756	9,127	9,350
Corporate Items (net)	85	64	178	376	441
Formula Grant	-2,767				
New Homes Bonus	-1,248				
Government funding		-3,614	-3,253	-3,253	-3,253
Use of New Homes Bonus	708	500	300	100	0
Transfer to/from(-) New Homes Bonus reserve	540	0	0	0	0
Transfer to Business Rates contingency	0	150	150	150	150
Transfers to/from(-) other Earmarked Reserves	-202	25	81	2	80
Transfer from Budget Equalization Reserve	-179	-146	-232	-184	-156
Council Tax Requirement	4,973	5,548	5,980	6,318	6,612
Council Tax income	-4,973	-5,148	-5,330	-5,518	-5,712
Savings Required	0	400	650	800	900

- 45 The summary shows that additional savings of £900,000 per annum need to be secured by 2016/17. This can be phased in during the next few years, with use of the Budget Equalization Reserve.

46 There is some flexibility given that the use of New Homes Bonus is entirely discretionary. For example, the budget could be balanced in 2013/14 by deciding to allocate £100,000 instead of £500,000.

47 **It is emphasised again that major uncertainty underpins these forecasts, in particular relating to Government funding as discussed above.**

48 The Council's capacity to achieve the level of savings necessary is discussed below under "Strategic Solutions".

Reserves

49 The Council is required to establish reserves to meet expected future financial commitments and to ensure a safe level of contingency in the event of unforeseen events.

50 The Council's policy, established in previous iterations of the MTFs, is to ensure that a Working Balance is maintained at a minimum safe contingency level equivalent to the sum of 2% of expenditure and 2% of income; around £1.2 million. This is subject to annual advice provided by the Section 151 Officer under Section 25 of the Local Government Act 2003.

51 Based upon the projected use of reserves included within the five year budget model, the following table sets out the forecasted reserve balances during the period covered by the MTFs.

Reserves £000	31-Mar-11	31-Mar-12	31-Mar-13	31-Mar-14	31-Mar-15	31-Mar-16	31-Mar-17
Working Balance	1,181	1,181	1,214	1,240	1,281	1,323	1,363
Change Management (note 2)	813	1,255	1,005	1,005	1,005	1,005	1,005
Planning	348	308	279	279	279	279	279
Landsanki Contingency (note 1)	702	-	-	-	-	-	-
Waste Management	222	220	150	150	150	150	150
Energy Efficiency	9	9	9	9	9	9	9
Licensing	139	92	41	-	-	-	-
Elections	62	26	46	66	86	26	46
Business Development	42	2	2	2	2	2	2
Housing Benefits	155	346	346	346	346	346	346
Homelessness	25	45	65	85	105	125	145
New Homes Bonus	-	214	754	754	754	754	754
Business Rates contingency	-	-	-	150	300	450	600
Council Tax Freeze Grant	-	-	125	125	125	125	125
Budget Equalization Reserve	1,499	1,400	1,221	1,075	843	659	503
TOTAL	5,197	5,098	5,257	5,286	5,285	5,253	5,327
1. Assumes no further write off adjustment required and balance on the reserve transfers to Change Management							
2. 31 March 2012 balance includes forecast net favourable variance for 2011/12 of £169,000.							

52 The table shows that total reserves stay reasonably constant during the MTFs period. The Working Balance increases steadily in line with established policy and a Business Rates contingency reserve is established, with the Budget Equalization Reserve reducing.

Strategic Solutions Workstreams

- 53 In 2009 the five workstreams were established and from 2010 a small corporate team was set up to secure the savings needed by the MTFS.
- 54 The workstreams have been successful to date, with cumulative annual savings of just under £1.9 million delivered for 2012/13. This is close the £2m savings target identified in previous iterations of the MTFS.
- 55 There is more to do however; cost inflation and decisions to make service investment erode the net savings position. The five year model show that additional savings of up to £900,000 are needed.
- 56 The workstreams table has been updated and is attached to this report. It shows that work is in hand or planned to deliver a level of savings slightly in excess of what is required. This is a sensible position as inevitably, some projects will not proceed as intended or may not deliver the expected level of savings. Also, unexpected cost pressures may arise, increasing the savings target.
- 57 The priorities for implementation are as follows:
- Implementing changes to the Waste service
 - Achieving a successful outcome from tendering the recycling gate fees contract
 - Securing Revenues & Benefits savings
 - Successful implementation of the IDOX ICT project.
 - Museum efficiency savings
- 58 The Council maintains a Change Management reserve to meet the one off costs of delivering the projects.

Decision making

- 59 Inevitably during the period of the MTFS, resource allocation decisions will be required based upon changing circumstances and priorities. Some budgets will need to be increased, and some reduced.
- 60 The Council will seek to safeguard those services that it considers to be highest priority as stated in the Corporate Plan.
- 61 The Council may make savings in priority areas only if there is no significant adverse impact to quality and level of service provision. For example, the Council may find a more efficient means of delivering the service, or partnership funding may be secured. Otherwise, the Council will not make savings that result in diminution in service quality in these areas unless there is absolutely no alternative e.g. inability to balance the budget.

- 62 The Council acknowledges the need to provide statutory services, and in many cases these will be consistent with Corporate Plan priorities. Where the link between the need to provide a statutory service and Corporate Plan priorities is not as strong, the Council will provide a level of service consistent with affordability. Efficiency gains and partnership working will be explored as means of providing statutory services to an acceptable level at a lower cost. In some circumstances, the Council will consider reducing the level of service in order to make savings and redirect resources to the Council's highest priorities.
- 63 Subject to the above, unavoidable and essential growth items will be funded by the making of savings from elsewhere within the Council budget, or the generation of additional income. The Council will manage its budget as a corporate whole, if necessary transferring money from one activity to another if this is what is necessary to match limited resources to the highest priorities.
- 64 In ordinary circumstances the Council will not use reserves to fund any ongoing expenditure. In exceptional circumstances, the Council may use reserves for one-off items or to alleviate budget pressures within the context of an overall plan to achieve a balanced budget but will seek opportunities to replenish reserves consumed in this way.

Risk Analysis

Risk	Likelihood	Impact	Mitigating actions
Actual experience differs from the assumptions in the budget and business plan	3 some variation is inevitable	3 sums involved are potentially significant	Ensure MTFS has element of flexibility Robust monitoring Half yearly review by Cabinet

1 = Little or no risk or impact

2 = Some risk or impact – action may be necessary.

3 = Significant risk or impact – action required

4 = Near certainty of risk occurring, catastrophic effect or failure of project.

**STRATEGIC SOLUTIONS WORKSTREAMS
UPDATED FEBRUARY 2012**

	Green shading <i>No shading, italics</i>	Saving secured and implemented <i>Decision made, awaiting implementation</i>						
		Examples	2011/12 £000	2012/13 £000	2013/14 £000	2014/15 £000	2015/16 £000	2016/17 £000
Workstream 1: Shared Services	Joining with other local authorities to deliver services in partnership and share costs or outsource to the private sector	Revenues and Benefits		30	190	190	190	190
		Workstream Total	-	30	190	190	190	190
Workstream 2: Devolution	Transferring services and assets to town/parish councils with UDC	TIC	10	10	10	10	10	10
		Toilets Dunmow	12	12	12	12	12	12
		Community assets SWTC	10	20	30	40	50	50
		Toilets Thaxted				23	23	23
		Workstream Total	32	42	52	85	95	95
Workstream 3: Income Generation	Maximising revenue from council assets	Car park tariff		114	114	114	114	114
		Building Control	51	51	51	51	51	51
		Pest Control			11	22	22	22
		Green Waste income		64	200	200	200	200
		Recycling gate fees		190	190	190	190	190
		Office rental			25	50	50	50
		Workstream Total	51	419	591	627	627	627
Workstream 4: Service Reduction	Stopping providing services or reducing contributions	Supaloos	71	71	71	71	71	71
		Gt Dunmow office sale	22	22	22	22	22	22
		Museum	30	40	60	77	77	77
		Toilets Felsted	5	5	5	5	5	5
		Solid Waste	16	16	16	16	16	16
		Workstream Total	144	154	174	191	191	191
Workstream 5: Efficiency savings	Ensuring that overheads are proportionate to the current business needs and size of the Council	Allowances	34	102	169	228	249	249
		Budget Slack	63	63	63	63	63	63
		Building Control		86	86	86	86	86
		Communications		19	19	19	19	19
		Concessionary Travel	30	30	30	30	30	30
		Credit cards		23	23	23	23	23
		CSC (R&B)	28	28	63	63	63	63
		External Audit		56	56	56	56	56
		Finance (R&B)	24	24	24	24	24	24
		Grounds Maintenance		38	38	38	38	38
		ICT (R&B)	39	79	79	79	79	79
		Idox			85	85	155	155
		Legal (R&B)	19	27	34	34	34	34
		Mailroom (R&B)	6	6	11	11	11	11
		Planning		47	47	47	47	47
		Printroom (R&B)	11	11	21	21	21	21
		Senior management	94	180	180	180	180	180
		Trade Waste		31	31	31	31	31
		Waste General		101	213	323	323	323
		Waste ZBB	266	266	266	266	266	266
		Workstream Total	614	1,217	1,538	1,707	1,798	1,798
Cumulative annual efficiency savings (as per budget)			841	1,862				
Additional savings identified in 2012/13 budget				1,021				
Forecasted cumulative annual efficiency savings					2,545	2,800	2,901	2,901
Additional cumulative annual savings above 2012/13					683	938	1,039	1,039
Savings target as per MTFS					400	650	800	900
Headroom / flexibility					283	288	239	139