Committee:	**Finance & Administration**	**Agenda Item**
Date:	**16 September 2010**	**13**
Title:	**Medium Term Financial Strategy** **Mid Year Review**	
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Summary

1. The Council approved the present Medium Term Financial Strategy (MTFS) "Strategic Solutions" in February 2010. The MTFS forecasted a progressively worsening in-year budget deficit during the next few years. The MTFS examined alternative scenarios for cuts in Government funding, from 0% to 30%, which culminated in an in-year deficit by the year 2014/15 of between £1.2 and £2.4 million. The 'base' assumption was a 10% cut, giving rise to a £1.6 million in-year deficit by 2014/15.
2. The assumptions underpinning the MTFS have been reviewed to take account of changing circumstances. There are material and significant uncertainties surrounding major items in the budget model such as staff pay, pensions costs, concessionary fares, land charges, Government funding and Council Tax. Landsbanki is another material uncertainty. This makes accurate forecasting difficult but on the basis that the assumptions are prudent and as realistic as possible, the big picture is unlikely to depart significantly from that set out in this report.
3. The key change in this mid-year review is a revised base assumption regarding Government funding. Based upon statements made by the Government as part of the June 2010 budget, it is now assumed that funding will be reduced by 25% during the next 4 years. This gives rise to an in-year deficit rising to £2.5 million by 2014/15.
4. The actual position with regard to Government funding will not be known until late November/early December.
5. The Strategic Management Board has identified a range of possible strategic solutions, grouped within five workstreams, to meet the savings targets. A corporate team is being established to implement the workstreams. One-off costs are likely to be incurred as part of this work, so the Council will need to ensure adequate funding for these via the Change Management Reserve.
6. Savings of £0.6 million are required for the forthcoming budget round, 2011/12, so early progress is needed to secure savings from the various workstreams.

Recommendations

7. The Committee is recommended to note and approved the revised financial forecasts as set out in this report.

Financial Implications

8. There are no direct financial implications arising from the recommendation. The report details the financial outlook for the Council for the next few years.

Background Papers

9. The following papers were referred to by the author in the preparation of this report and are available for inspection from the author of the report.

   Medium Term Financial Strategy

   2010/11 Budget Book

   Government Budget announcements June 2010

Impact

Communication/Consultation	None
Community Safety	None
Equalities	None
Health and Safety	None
Human Rights/Legal Implications	It is a legal requirement that the Council sets a balanced budget.
Sustainability	None
Ward-specific impacts	None
Workforce/Workplace	Implementing Strategic Solutions workstreams will have implications for the workforce. These will be identified and addressed on a project-by-project basis.

Medium Term Financial Strategy – Review of Key Assumptions

Local Government Finance Settlement

10. The Government has indicated that average public sector spending will be cut by 25% in real terms (i.e. after adding inflation). Government Departments have been asked to look at scenarios of up to 40%.

11. A 25% cut in real terms (with inflation) is equivalent to an 18% cut in cash terms.

12. The Comprehensive Spending Review is not due to report until October, so as yet there is no information about what reduction will be suffered by local government, or within local government, what reductions will be experienced by district councils. Allocations for individual councils will not be known until late November/early December. It is possible that cuts higher or lower than 25% will be experienced at individual council level.

13. The revised MTFS uses a base assumption of a 25% cash cut implemented in equal instalments over the next 4 years i.e. 6.25% per year from 2011/12 to 2014/15.

14. There are indications that the Government may publish a 2 year settlement (covering 2011/12 and 2012/13); if so, uncertainty over the medium term will continue.

Concessionary Fares Adjustment

15. From 2011/12, responsibility for concessionary fares transfers to upper tier authorities, i.e. Essex County Council in our case. The MTFS therefore removes all budgeted spend (approx £0.3 million) and specific grant income (£0.1 million) from 2011/12 – a net cost reduction of £0.2 million per year.

16. However, a reduction is to be made to the Council's RSG funding from Government, as an element of the RSG relates to Concessionary Fares (although it is not possible to accurately quantify this).

17. It has generally been the case that rural authorities with underdeveloped public transport have fared well under the existing system: the RSG funding is thought to exceed the costs incurred. Conversely, predominately urban authorities have fared badly, with costs exceeding the RSG allocation. This perceived unfairness is one of the main reasons for the forthcoming transfer to upper tier authorities, and will enable disparities at district level to be smoothed over a wider area.

18. However, the implications for UDC are potentially serious: the reduction in RSG will be more than the budget saving. The Government is consulting on 4 different options for making the adjustment: the exemplifications provided quantify the reductions as £0.4 million, £1 million, £0.4 million and £0.6 million. There are indications that the Government favours the third option, therefore, the MTFS assumes a reduction in RSG funding of £0.4 million from 2011/12.

This is over and above any cut that might emerge from the Comprehensive Spending Review.

19. This means that the in-year position is worsened by approximately £0.2 million. There is a risk that the worsening could be as much as £0.4 to 0.8 million, if the Government implements either option 2 or option 4.

20. Analysis shows that 10 out of 12 Essex districts fare best under options 1 and 3, which produce very similar results. 1 district, the predominately urban Harlow, fares best under option 2, and 1 district, Colchester, fares best under option 4.

Council Tax

21. The Government has indicated that they will freeze Council Tax in 2011/12 "in partnership with local authorities". The method by which this will be accomplished has not been published.

22. The MTFS assumes that there will be Council Tax rise in 2011/12, and that the Government will make a one-off funding contribution equivalent to a 2.5% increase.

23. From 2012/13, the MTFS assumes an annual rise of 2.5%.

24. An annual taxbase increase of 1% is assumed.

Staff Pay Award

25. The MTFS assumes that increments will continue to be paid to staff who are entitled to receive them.

26. The Local Government Employers side is maintaining its position that there will be no cost of living pay award in 2010/11, and are refusing to negotiate. Unions are unhappy with this position, and disputes are likely. The MTFS assumes that the Employers' position will prevail.

27. The Government has indicated that there will be a public sector pay freeze in 2011/12 and 2012/13, apart from pay rises of £250 in each year for staff earning under £21,000. The MTFS is based on this position. It is not yet clear whether this policy will apply to local government.

28. A 1% pay rise per year in 2013/14 and 2014/15 has been assumed.

29. The MTFS assumes that Members Allowances will increase (or not, as the case may be) in line with assumptions about the staff pay award.

Pension Fund Deficit

30. The Essex Pension Fund is currently undergoing its triennial revaluation to accurately quantify the deficit and determine a funding strategy that will be implemented in 2011/12. Indicative results are to be shared at an Employers Forum meeting on 14 September; a verbal update will be provided at the F&A

Committee meeting. Detailed implications for each employer will not be available until later in the Autumn.

31. It is anticipated that the Pension Fund deficit will have increased and that this will have cost implications for Councils. Implications could be mitigated by, for example, the Actuary specifying a longer deficit recovery period. Nevertheless, an increase in annual contribution is likely.

32. The latest estimate available suggests that an increase in the region of 1.3% of pay may be required, rising by a further 1.3% each year. The MTFS is based on this assumption.

33. A detailed report about the Pension Fund deficit is being considered by the Performance Select Committee on 21 September, in connection with approval of the 2009/10 Statement of Accounts.

Land Charges

34. The position with regard to land charges income continues to be uncertain. Although a Statutory Instrument has been enacted, which means that charges may not be levied for personal searches, uncertainty remains about other search fee income. The MTFS prudently assumes that income shall be nil, but it is possible that the situation, once clarified, will be better than this.

Interest Rates

35. Forecasts for investment income and capital financing costs are based on interest rate predictions supplied by Arlingclose. The estimates currently assume that the base rate will remain at 0.5% until June 2011, then increase steadily until it reaches 3% by March 2013.

Fees & Charges Income

36. The model assumes no change in the level of income received from car parking, planning fees and building control fees.

37. At this stage no assumption has been built into the model relating to any changes in income levels arising from adopting a new Pricing & Concessions Policy, pending a detailed financial evaluation. Experience in one service where elements of the policy have been trialled suggest a modest increase in income, but the situation will differ from service to service.

Landsbanki

38. Details of the recoverable amount are unlikely to be known until Spring 2011. A contingency fund of £1.2 million has been established; the amount potentially at risk is £2.3 million, although LGA/CIPFA advice is to assume a 95% recovery. The MTFS assumes no additional provision will need to be made above the contingency fund already established. Clearly in a worst case scenario, there will be a substantial additional write off which would require a revision of the MTFS.

Other Inflation Assumptions

39. For items not specified above the MTFS makes the following generic assumptions:

Utilities costs	10% price inflation per year
Supplies & services subject to contractual indexation	2.5% inflation in 2011/12; 2% per year thereafter
Supplies & services not subject to contractual inflation	0% inflation
Income from fees & charges	1.5% inflation in 2011/12; 2% per year thereafter
Housing & Council Tax Benefits expenditure	Housing Benefit (private tenants) – 3% inflation per year. 10% case load increase in 2011/12, 5% per year thereafter. Rent Rebates (council tenants) – 3% inflation per year. No caseload increase. Council Tax Benefit – 0% inflation in 2011/12, 2.5% per year thereafter. 5% increase in caseload per year.
Housing & Council Tax Benefits Government Subsidy	Assumed that 98% of expenditure will be recovered
Housing & Planning Delivery Grant, LABGI, Area Based Grant	Nil
Recharge to Housing Revenue Account	No change

Sensitivity Analysis

40. The following shows the effect on the 2011/12 projections of a 1% variance from the assumptions made.

Staff pay (& oncosts)	£82,000
Supplies & services (contractual)	£39,000
Supplies & services (non-contractual)	£16,000
Utilities costs	£6,000
Fees & charges income	£40,000
Housing & Council Tax Benefits Government Subsidy	£184,000
Local Government Finance Settlement	£41,000
Council Tax	£49,000
Interest Rates (additional income if base rate is 1% above prediction)	£144,000

Summary of 5 year model

41. The revised MTFS model is shown below. It shows a gap between budget and available funding of £0.9 million in 2011/12, rising to £2.5 million by 2014/15. After making use of the Budget Equalization Reserve, the savings target for 2011/12 is £0.6 million, rising to £2.2 million by 2014/15.

	2010/11	2011/12	2012/13	2013/14	2014/15
	Budget	Forecast	Forecast	Forecast	Forecast
	£m	£m	£m	£m	£m
Gross Service Expenditure	32.770	33.947	35.341	36.887	38.534
Income	-23.512	-24.785	-25.979	-27.268	-28.647
Net Service Expenditure	**9.257**	**9.162**	**9.362**	**9.619**	**9.888**
Recharge to HRA	-0.930	-0.930	-0.930	-0.930	-0.930
Contribution towards overheads by HRA	-0.267	-0.267	-0.267	-0.267	-0.267
Landsbanki Impairment	1.162	0.000	0.000	0.000	0.000
Investment income	-0.072	-0.084	-0.285	-0.350	-0.315
Capital financing costs	0.834	0.887	0.962	0.986	1.328
Pension Fund Deficit	0.465	0.554	0.644	0.736	0.828
Net Operating Expenditure	**10.449**	**9.323**	**9.487**	**9.794**	**10.531**
Transfer to General Fund Working Balance	0.085	0.048	0.059	0.060	0.069
Net transfers to/from(-) earmarked reserves	-1.239	0.030	0.030	0.030	0.030
NET BUDGET REQUIREMENT	**9.295**	**9.401**	**9.576**	**9.884**	**10.630**
Funding available					
Local Government Finance Settlement	4.106	3.849	3.593	3.336	3.080
LGFS adjustment for concessionary fares	0.000	-0.385	-0.385	-0.385	-0.385
Area Based Grant	0.026	0.000	0.000	0.000	0.000
Council Tax	4.853	4.902	5.074	5.253	5.438
Compensation for Council Tax Freeze	0.000	0.123	0.000	0.000	0.000
Collection Fund balance	-0.023	0.000	0.000	0.000	0.000
TOTAL FUNDING AVAILABLE	**8.962**	**8.488**	**8.282**	**8.204**	**8.133**
In year deficit	**0.333**	**0.912**	**1.294**	**1.679**	**2.498**
Transfer from Budget Equalization Reserve	-0.333	-0.312	-0.194	-0.179	-0.298
Savings Target	**0.000**	**0.600**	**1.100**	**1.500**	**2.200**

42. The model will be kept under review and significant changes reported to Members. The MTFS document, fully revised, will be presented to this Committee and the Full Council in February as part of the 2011/12 budget approval process.

Strategic Solutions Workstreams

43. The required savings are to be delivered by means of Strategic Solutions Workstreams. An illustration of how this will work in practice is attached to this report. The figures represent SMB's estimate of the savings that will materialise from work that is already in hand, or envisaged. This is an evolving situation so the actual list of projects and attributable savings are subject to change.

44. The imperative for the Council is to make early and significant progress towards securing the level of savings required. The model requires £0.6 million of savings to be identified as part of the 2011/12 budget, i.e. by February 2011. Progress has to be sustained at a good rate for the next few years.

45. Securing the savings will entail a significant amount of capacity that cannot be accommodated alongside everyday duties. Accordingly a corporate team is being established by means of internal secondment, with backfilling of the secondees being resourced from the Change Management Reserve.

46. Implementing the Workstreams will entail one-off costs so the Council will need to ensure that the Change Management Reserve is sufficiently resourced during the life of the MTFS. Subject to developments in the Landsbanki issue, favourable variances and/or uncommitted reserves that become available should be diverted to Change Management.

47. Members will received regular progress report on the status of the Workstreams and the level of secured savings.

Risk Analysis

Risk	Likelihood	Impact	Mitigating actions
Assumptions are too optimistic, or too prudent	3 (given the significant uncertainties, some assumptions will be proved, with the benefit of hindsight, to be incorrect)	3 (the target level of savings will need to be revised)	Keep assumptions under review and revise MTFS regularly
Insufficient progress made to secure the level of savings required	2 (resources are being invested)	4 (the Council will become financially unstable, necessitating short-term measures rather than Strategic Solutions)	Establish Corporate Team Regular progress reports to Members Section 151 Officer responsibility to report on the robustness of estimates and adequacy of reserves

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.

			2010/11 £000	2011/12 £000	2012/13 £000	2013/14 £000	2014/15 £000
Workstream 1: Shared Services or Outsourcing	Joining with other local authorities to deliver services in partnership and share costs or outsource to the private sector	Revs & Benefits	0	85	170	170	170
		Planning	0	0	100	200	200
		Waste and Recycling	0	50	50	50	50
		Shared Depot	0	10	20	20	20
		ICT	0	0	0	25	50
		Internal Audit	0	0	6	12	12
		Legal	0	0	6	13	13
		Finance	0	0	25	50	50
		Workstream Total	**0**	**145**	**377**	**540**	**565**
Workstream 2: Devolution	Transferring services and assets to town/parish councils with UDC funding provided on a reducing basis	TIC	0	10	10	10	10
		Toilets Dunmow	3	5	8	10	10
		Community assets SWTC	0	14	29	43	58
		Museum	0	30	60	100	160
		Workstream Total	**3**	**59**	**107**	**163**	**238**
Workstream 3: Income Generation	Maximising revenue from council assets	Car park tariff	0	0	80	160	160
		Reduce subsidy of Pest Control	0	8	17	17	17
		Renting out accommodation	0	0	15	30	30
		Workstream Total	**0**	**8**	**112**	**207**	**207**
Workstream 4: Service Reduction	Stopping providing services or reducing contributions	Supaloos	0	80	80	80	80
		Saving at Gt Dunmow	0	24	24	24	24
		Toilets Felsted	3	3	3	3	3
		Procurement/Asset Management	0	25	50	75	100
		Workstream Total	**3**	**132**	**157**	**182**	**207**
Workstream 5: Efficiency savings	Ensuring that overheads are proportionate to the current business needs and size of the Council	Senior management	40	85	85	85	85
		ICT (R&B)	0	80	80	80	80
		Printroom (R&B)	0	21	21	21	21
		Finance (R&B)	0	23	23	23	23
		Legal (R&B)	0	34	34	34	34
		CSC (R&B)	0	63	63	63	63
		Mailroom (R&B)	0	11	11	11	11
		Building Control	30	72	72	72	72
		Budget Slack	0	200	200	200	200
		Ess User/Lease Car	0	30	60	100	100
		UDC Allowance	0	3	6	9	12
		Workstream Total	**70**	**622**	**655**	**698**	**701**
		TOTAL SAVING £000	**76**	**966**	**1,408**	**1,790**	**1,918**
		TARGET SAVING £000	**0**	**600**	**1,100**	**1,500**	**2,200**
		SAVING ABOVE/BELOW(-) TARGET	**76**	**366**	**308**	**290**	**-282**