

TONBRIDGE & MALLING BOROUGH COUNCIL

CABINET

12 October 2011

Report of the Director of Finance and the Cabinet Member for Finance

Part 1- Public

Executive Non Key Decisions

1 MEDIUM TERM FINANCIAL STRATEGY AND INITIAL BUDGETARY GUIDANCE

To consider factors that are likely to impact on the Council's finances for both the forthcoming budget cycle and Medium Term Financial Strategy and to seek endorsement to the Budgetary Guidance issued to staff for the 2012/13 budget cycle.

1.1 Introduction

- 1.1.1 The Council's Medium Term Financial Strategy covers both revenue and capital budgets, and it is this Strategy that underpins the budget setting process for the forthcoming year and over the strategy period.
- 1.1.2 The aim of the Medium Term Financial Strategy is to give us a realistic and sustainable plan that reflects the Council's priorities and takes us into the future. Since it was introduced in 2003 **the Medium Term Financial Strategy has been instrumental in protecting the services that are provided by the Council and it has enabled us to take a more measured approach than would have been possible without it.** However, it is not a panacea which can insulate the Council from the severe cuts in government funding.
- 1.1.3 Given the scale of the financial challenge faced by the Council as part of the 2011/12 budget setting process we moved to a Medium Term Financial Strategy spanning a ten-year period; and set the following two fundamental objectives: to maintain a minimum general revenue reserve balance at £2.0m and to achieve a balanced budget by the end of the strategy period.
- 1.1.4 The Strategy also sets out based on current financial information, not only the projected budgets for the period, but also the levels of council tax that are projected to be required to meet the Council's spending plans. Underneath the Strategy for the budget setting year sits detailed estimates formulated in conjunction with Services taking into account past outturn, current spending plans and likely future demand levels / pressures.

1.1.5 The Medium Term Financial Strategy itself is the Council's high level financial planning tool and will need to be refreshed, updated and rolled forward as part of the 2012/13 budget setting process.

1.1.6 Members are fully aware that this is a time of significant change for local government, and the public sector as a whole in the light of the current economic climate. The financial difficulties the entire public sector is facing are unprecedented, but we believe our Medium Term Financial Strategy is resilient and the financial pressures likely to confront us can be addressed in a measured and controlled way. Clearly, the absolute size of the 'funding gap' will influence the timescales we afford ourselves to address the problem.

1.2 Medium Term Financial Strategy

1.2.1 It is probably worthwhile just reminding ourselves of the objectives currently set out in the Medium Term Financial Strategy.

- To achieve a **balanced revenue budget** that delivers the Council's priorities by the end of the strategy period.
- To retain a **minimum of £2.0m** in the General Revenue Reserve by the end of the strategy period.
- For 2011/12, freeze the council tax at 2010/11 levels; and thereafter seek to set **future increases in council tax having regard to the guidelines** issued by the Secretary of State.
- Over the strategy period, **continue to identify efficiency savings** within the Council's budget to contribute towards the identified 'funding gap'; and, if necessary thereafter, **seek appropriate reductions in service costs** following consultation, as necessary, with taxpayers.
- Set a **maximum 'annual capital allowance'** each year as part of the budget setting process for all new capital schemes (for 2011/12 set at £350,000 from the Council's own resources) and give priority to those schemes that generate income or reduce costs.

1.2.2 As ever, there are numerous factors that need to be taken into account when updating the Strategy. Some of the more significant factors that are likely to impact on the Council's finances in the forthcoming budget round and over the period of the medium term are given below.

Energy Prices

1.2.3 The extreme volatility in energy prices remains. This volatility clearly makes budgeting difficult. Members will be aware that the Council is a member of an energy consortium where the contractual arrangements are managed and administered by Kent Commercial Services (Laser). As a result of this

arrangement the recent hike in energy prices of between 15 to 20 per cent have not yet impacted on the Council's energy costs, but will in due course if energy prices remain at their current levels. To put this into context, a 10% movement in energy prices would equate to about £70,000.

Inflation

- 1.2.4 The Consumer Prices Index is currently running at 4.5% (August) and the Retail Prices Index at 5.2% (August). Most of the Council's major contracts are uplifted annually by the Retail Prices Index.
- 1.2.5 The Government's inflation target is presently 2% and is based on the Consumer Prices Index (CPI). As Members may be aware, the Bank of England's Monetary Policy Committee aims to set interest rates so that inflation can be brought back to target within a reasonable time period without creating undue instability in the economy.
- 1.2.6 Latest predictions suggest that inflation will remain stubbornly high over the next twelve months. Accordingly, we are minded to update the Medium Term Financial Strategy assuming a general uplift for inflation of 4% in 2012/13 and 3% in 2013/14 and 2% in subsequent years. To put this into context, 1% on our major contracts (e.g. refuse collection, grounds maintenance, street cleaning) would equate to about £40,000.

Investment Income

- 1.2.7 The Medium Term Financial Strategy approved by Members as part of the 2011/12 budget cycle anticipated an investment return on our 'core funds' of 1.4% in 2011/12 before rising gradually to 5.0% by the end of the strategy period.
- 1.2.8 The Bank of England bank rate is now expected to remain at 0.5% for longer than anticipated when the 2011/12 budget was set and the fact that the bank rate is predicted to remain at an historic low for longer will clearly impact on our investment income at least in the short term.
- 1.2.9 To put this into context, 1% would currently generate investment income of about £230,000.
- 1.2.10 The deposit of £1m invested in the Icelandic Bank Landsbanki has not yet been repaid in full or in part. Investment income projections currently assume repayment of £180,000 in each of the five years 2015/16 to 2019/20 and we will need to revisit this assumption in updating the Strategy to reflect the latest developments and information available.

Economic Climate

- 1.2.11 Our major income streams continue to suffer due to the current economic climate. Members will recall that this time last year we assumed that after taking into account of action to reduce costs in related areas there would remain a net shortfall of £1,125,000 and that the economy will have recovered part way through 2014/15.
- 1.2.12 Latest forecasts and projections would suggest that the economic downturn is to be more protracted than originally envisaged, and of more concern is that it is becoming apparent that we have seen a **permanent** rather than temporary reduction in some of our major income streams due to changes in behaviour and or competition and the implications this has for the Medium Term Financial Strategy and the size of the 'funding gap'.
- 1.2.13 For this reason income estimates will in future be based on current income levels rather than what has been referred to as a 'normal' level of activity. This will require us to reflect within the Medium Term Financial Strategy an increase in income levels when the economy improves and confidence returns, but when this will be and to what extent is difficult to forecast. Members are also advised that increased customer use of Freedom of Information (FOI) and Environmental Information (EiR) Regulations may impact on a range of income streams over the life of the MTFs and the Management Team will continue to monitor this.
- 1.2.14 In terms of the council tax base, we have continued to assume growth in the number of band D equivalents based on the 'average' growth over the past few years. Members will also be aware that this 'growth' (or otherwise) will impact on the level of the New Homes Bonus that the Council might receive in the future.
- 1.2.15 It is important to recognise, however, that, currently, the timing of development growth is very difficult to predict given the market as well as other site specific conditions. Therefore, our assumption about the growth in taxbase comes with a 'health warning' and we ask Members to note that we will be keeping development progress under close review as we move forward.

Leisure Services Business Unit

- 1.2.16 Members were advised at the meeting of the Finance and Property Advisory Board in July that the Business Unit to the end of June was trading **below profile** by more than £100,000 after having taken into account the economic downturn adjustment (the latest update reported to the Leisure & Arts Advisory Board on 21 September suggests that for the year this figure will be in the order of £225,000). Clearly, if this pattern of trading continues it will place further budgetary pressure on the Council's finances.

General Government Grant

- 1.2.17 The Council is to see its grant funding cut by more than 28% over the two-year period 2011/12 to 2012/13 with further cuts expected in future years. The Medium Term Financial Strategy assumes further cuts of 0.9% and 5.6% in 2013/14 and 2014/15 respectively and thereafter increasing by 2% each year. What is of some concern is the fact that growth predictions have been lowered in recent months and will this result in cuts to grant funding of more than that assumed above.
- 1.2.18 However, elsewhere on this agenda is a report outlining the main proposals set out in the consultation paper: Proposals for Business Rates Retention which if introduced would replace Formula Grant funding.

Local Government Resource Review: Proposals for Business Rates Retention Consultation Paper

- 1.2.19 As mentioned above a separate report on this consultation paper can be found elsewhere on this agenda. Under the proposals funding above a minimum amount is dependent on growth in an authority's business rates base which clearly makes it difficult to predict future funding levels for medium term financial planning purposes. It can be envisaged that under such a system in some years an authority would 'do well' and in others 'not so well' (funding would be 'lumpy'), but that over the medium to long-term there will be a large group of authorities for whom the change does not make a great difference.
- 1.2.20 What is likely, however, is that a greater amount of financial 'risk' will be passed over to local authorities, and therefore it will be imperative that councils have sufficient levels of reserves to tide them over during any 'bad' times.

Localising Support for Council Tax in England Consultation Paper

- 1.2.21 Elsewhere on this agenda is a report outlining the main proposals set out in the consultation paper: Localising Support for Council Tax in England. The Government announced in the Comprehensive Spending Review 2010 that support for council tax will be localised from 2013/14 and expenditure reduced by ten per cent. Clearly, this could have significant financial implications depending on the grant award compared to the cost of the localised scheme.
- 1.2.22 At the present time, it is central government that bears the risk associated with fluctuations in council tax benefit increases (or decreases). If the proposals made in the consultation paper are agreed in due course, the risk will pass to local authorities and so if caseload increases councils will need to bear the costs from their own budgets. In a similar way to the business rates proposals above, it will be imperative that councils have sufficient levels of reserves to tide them over during any 'bad' times.

Localised Setting of Planning Fees

1.2.23 The local setting of planning fees may generate additional income over and above the sums currently reflected within the Medium Term Financial Strategy. However, this will be dependent on the details of the arrangements which are awaited, as is the passing of the Regulations giving local authorities the power to set planning fees.

1.3 Budgetary Guidance for 2012/13 Budget Cycle

1.3.1 What with, amongst other things, inflation remaining stubbornly high, the expected hike in energy prices and that we have seen a permanent rather than temporary reduction in some of our major income streams is leading me to become increasingly concerned about the savings (size of the 'funding gap') we need to make and how this is going to be addressed. The latest publicised 'funding gap' is £2m, but we are fearful that many of the factors outlined above have only served to put further upward pressure on the size of the 'funding gap'.

1.3.2 Indeed, early consideration of the factors that are likely to impact on the Council's finances for both the 2012/13 budget cycle and over the medium term suggest a 'funding gap' in the order of £2.9m (after some immediate savings of circa £300,000 have been realised – see paragraph 1.3.6 below). As in previous iterations of the Medium Term Financial Strategy we could, **for example**, breakdown the savings target into tranches. An updated version of the Medium Term Financial Strategy is attached at **[Annex 1]** which breaks the savings target into four equal tranches of £725,000 to be achieved by 2013/14, 2014/15, 2016/17 and 2017/18. This version also assumes that we will deliver savings of £300,000 as part of the 2012/13 budget cycle as a result of implementing Stage 1 and Stage 2 below (paragraph 1.3.3 refers). Clearly, this is an **early projection** of the Medium Term Financial Strategy which will be updated as we move through the 2012/13 budget cycle and as more information becomes available.

1.3.3 For this reason the Director of Finance recently presented a report to Management Team setting out a three stage approach to begin tackling the significant financial challenge faced by the Council.

- Stage One – adjust budgets on the back of our continuous establishment reviews and most particularly on the back of our decision regarding the demise of the economic downturn adjustment.
- Stage Two – review of all budget lines when completing budget estimates for 2012/13 with the aim of reducing costs wherever possible.
- Stage Three – will be the more radical steps we need to take in order to address the budget 'funding gap'.

- 1.3.4 In addition, in consultation with Management Team, the Director of Finance has had no choice, but to again impose a cash limit on 2012/13 expenditure (at the same level as the current 2011/12 budget) and indeed to identify cost savings as opposed to cash standstill wherever possible and reiterated the objective to maximise income subject to market conditions, opportunities and comparable charges elsewhere.
- 1.3.5 In terms of contractual commitments many of our major contracts are uplifted annually by RPI. The Council has no choice, but to meet these increases as informed by the official RPI statistics.
- 1.3.6 Having regard to Stages One and Two of the process set out above, the Director of Finance anticipates that, with the assistance and cooperation of the Management Team, a sum of at least £300,000 will have been “shaved out” of the base ‘draft’ budget prior to it being presented to Members early in the New Year. Members should note that the achievement of this ‘target’ has already been factored into the MTFs update presented to this meeting, and the calculation of the ongoing funding gap of £2.9m described in paragraph 1.3.2 above.

1.4 Legal Implications

- 1.4.1 There are a number of legislative requirements to consider in setting the budget which will be addressed as we move through the budget cycle.

1.5 Financial and Value for Money Considerations

- 1.5.1 As set out above.

1.6 Risk Assessment

- 1.6.1 The Local Government Act 2003 requires the Chief Finance Officer, when calculating the Budget Requirement and Council Tax Requirement, to report on the robustness of estimates included in the budget and the adequacy of the reserves for which the budget provides. Consideration will and is given to the risks associated with any budget setting process where various financial and other assumptions have to be made. To mitigate the risks detailed estimates are formulated in conjunction with Services taking into account past outturn, current spending plans and likely future demand levels / pressures and external advice on assumptions obtained where appropriate.
- 1.6.2 The Medium Term Financial Strategy sets out the high level financial objectives the Council wishes to fulfil and underpins the budget setting process for the forthcoming year and over the strategy period. As the Council’s high level financial planning tool the Strategy needs to be reviewed and updated at least annually.

1.7 Equality Impact Assessment

1.7.1 See 'Screening for equality impacts' table at end of report

1.8 Recommendations

1.8.1 Members are **RECOMMENDED** to:

- 1) Note and endorse the content of the report and the decision to dispense with the economic downturn adjustment.
- 2) Endorse the budgetary guidance issued to Chief Officers preparing and considering estimates and fees and charges for 2012/13 (paragraph 1.3 refers).

Background papers:

contact: Sharon Shelton

Nil

Neil Lawley

Sharon Shelton
Director of Finance

Martin Coffin
Cabinet Member (Finance)

| Screening for equality impacts: | | |
|---|--------|--|
| Question | Answer | Explanation of impacts |
| a. Does the decision being made or recommended through this paper have potential to cause adverse impact or discriminate against different groups in the community? | Yes | Some changes to budgets may have potential to cause adverse impact and where this is deemed to be the case an equality impact assessment has or will be undertaken at the appropriate time. With regard to new capital plan schemes an equality impact assessment is to be undertaken and reported to Members prior to commencement of the scheme. |

| Screening for equality impacts: | | |
|---|---------------|--|
| Question | Answer | Explanation of impacts |
| b. Does the decision being made or recommended through this paper make a positive contribution to promoting equality? | Yes | This report sets out draft proposals in respect of the Budget for the forthcoming year within the context of the Medium Term Financial Strategy and the Council's priorities. As mentioned above changes to budgets where there are deemed to be equality issues an equality impact assessment has or will be undertaken at the appropriate time. In addition, an equality impact assessment is to be undertaken and reported to Members prior to commencement of a new capital plan scheme. |
| c. What steps are you taking to mitigate, reduce, avoid or minimise the impacts identified above? | | See responses above. |

In submitting this report, the Chief Officer doing so is confirming that they have given due regard to the equality impacts of the decision being considered, as noted in the table above.