

## TONBRIDGE &amp; MALLING BOROUGH COUNCIL

## CABINET

08 November 2022

## Report of the Director of Finance and Transformation

## Part 1- Public

## Executive Non Key Decisions

**1 MEDIUM TERM FINANCIAL STRATEGY AND SAVINGS UPDATE**

A report updating on the Medium Term Financial Strategy having regard to the latest financial issues. In addition, the report sets out the savings that have been identified and will assist in meeting 'tranche 1' of the latest savings target. Cabinet is requested to consider and implement a programme for investigating and identifying the balance of the savings that are needed to ensure the financial sustainability of the Council.

**Dashboard/ Key Points**

- Interim review of Funding Gap, representing new savings that need to be identified and most importantly delivered, now projected at between £2.6m at best case to £3.8m at worst case.
- Savings target "tranche 1" of £350k needs to be in place by April 2023. So far £164k achieved.
- To ensure future financial stability, Council needs to be able to respond to a worst case scenario, but in any event needs to prepare to deliver £1.5m within the next 3 years.
- Current turmoil in economic climate and financial markets, with inflation at highest level for many years, and Bank of England interest rate at highest level since 2008.
- Uncertainty regarding local government finance settlement, Fair Funding Review, Negative RSG, New Homes Bonus cessation and Business Rates baseline reset making it difficult to assess the true position.
- Budget position categorised as RED on the Strategic Risk Register.

## 1.1 Introduction

- 1.1.1 I updated the Cabinet on 7 June 2022 under the report “Revenue and Capital Outturn 2021/22” on the changing position of the Medium Term Financial Strategy (MTFS).
- 1.1.2 In that report I advised that the conflict in Ukraine had sparked an escalation in inflation and energy prices far beyond any forecasts. It had, of course, been hoped that the national economy would start to recover after the devastating impacts of the global pandemic. As a result, I reported that whilst it was very difficult at that point to give an indication of what this means for our “funding gap” within the MTFS, the general sense was that it might sit somewhere between £2.5m and £3.0m, although it could be more. This compared to the £2.15m ‘gap’ that had been referenced when the Budget was set in February 2022.
- 1.1.3 By the time I reported to Cabinet in July with a report entitled “Financial Planning and Control”, the estimated gap had increased to the £3.0m level. As I said then, the impact of surging inflation is not unique to Tonbridge and Malling and, unless the government recognise the scale of the pressure in future finance settlements and council tax referendum principles, it will be no surprise if a number of councils finances are under severe strain – including this Council.
- 1.1.4 Given this backdrop it is **essential** that we identify and achieve this year’s savings target of £350,000 by the start of the 2023/24 year. To this end Cabinet at its meeting in June Cabinet resolved that *“in order to ensure that the target of £350,000 is achieved by the start of the financial year 2023/24, a comprehensive report detailing all strands of work being undertaken in respect of the Savings and Transformation Strategy, including progress being made on achieving targets and outcomes be presented to Cabinet in November 2022”*.
- 1.1.5 This report therefore has two purposes:
- 1) it provides another update to the MTFS as the budget cycle for 2023/24 gets underway;
  - 2) it reports on the savings that have been secured thus far which contribute to “tranche 1” of the savings target.

## 1.2 The Medium Term Financial Strategy

- 1.2.1 Cabinet is reminded that the Medium Term Financial Strategy (MTFS) covers both revenue and capital budgets over a rolling ten-year period, and it is this Strategy that underpins the budget setting process each year and over the strategy period.
- 1.2.2 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.

1.2.3 The MTFFS sets out the high level objectives the Council wishes to fulfil over the agreed time span. These are:

- To achieve a **balanced revenue budget** that delivers the Council's priorities by the end of the strategy period.
- To retain a **minimum of £3.0m** in the General Revenue Reserve by the end of the strategy period and **not to fall below £2.0m** at any time during the 10-year period.
- Seek to set future increases in council tax having regard to the **guidelines** issued by the Secretary of State.
- Continue to **identify efficiency savings** and **opportunities for new or additional income sources** and to **seek appropriate reductions in service costs** in delivery of the Savings and Transformation Strategy (STS) approved by Members.
- Subject to there being sufficient resources within the capital reserve, set a **maximum 'annual capital allowance'** each year as part of the budget setting process for all new capital schemes (currently set at £250,000 from the Council's own resources) and give priority to those schemes that generate income or reduce costs.

1.2.4 The MTFFS is supported by the Savings and Transformation Strategy (STS). The purpose of the STS is to formulate an overarching plan as to how the "funding gap" identified within the MTFFS can be addressed.

### 1.3 Economic Situation

1.3.1 The Audit Committee, under the regular Treasury Management report, receives detailed information about the economic background, and it is not the intention to repeat this here.

1.3.2 However, it is worth noting that at the time of writing this report, CPI inflation for the year to end of August was 9.9%. When the Budget for 2022/23 was set in February this year, the Bank of England's forecasts for inflation were based around a level of 2% - demonstrating what an impact the Ukraine conflict and energy crisis is having.

1.3.3 On 22 September, The Bank of England raised interest rates by half a percentage point to 2.25% - the highest level since November 2008. The Bank anticipates that inflation will reach a peak slightly below 11% in October.

1.3.4 Without going into the details, the (then) Chancellor Kwasi Kwarteng set out a mini-budget on 23 September in which he announced how the government plans to deliver the tax cuts that the new Prime Minister promised during her leadership campaign to help people with the rising cost of living. As we know, many of the proposals made in that mini-budget have since been withdrawn as a result of the market reaction which followed. Nevertheless the market is still volatile.

## 1.4 Impact on Tonbridge & Malling Borough Council's MTFS

1.4.1 The Council's financial plans are significantly affected by the turmoil in the economic markets. Whilst this will certainly not be the last update of the MTFS before the budget is set for 2023/24, it is nevertheless important that Members are updated with the "***direction of travel***" so that plans can be formulated and implemented wherever necessary.

1.4.2 The problem is, of course, that there is uncertainty about many things. These include:

- Speed and rate at which inflation returns to levels more akin to that assumed when the budget was set in February 2022
- Local government finance settlement
- Fair Funding Review and future of New Homes Bonus
- Timing of Business Rates Retention "reset"
- Confirmation as to the permitted increase in council tax (without undertaking a referendum) for 2023/24

1.4.3 Of course, the impact of surging inflation is not unique to Tonbridge and Malling and, unless the government recognise the scale of the pressure in future finance settlements and council tax referendum principles, it will be no surprise if a number of councils finances are under severe strain – including this Council.

1.4.4 Members are aware that the largest single aspect of the revenue budget is the cost of staff. The Local Government Pension Scheme (LGPS) is a statutory public service scheme (*for which the benefits and terms are set out in regulations passed through parliament*) and all employees are entitled to join the scheme. The LGPS is administered through regional pension funds, and locally the Kent Pension Fund is the regional fund with Kent County Council as the administering authority.

1.4.5 Every three years the actuary carries out a valuation of the Pension Fund, with an objective of monitoring the assets of the Fund against the liabilities of the pension benefits payable. As a result of this valuation, individual employers' contribution rates to be paid for the following three years are determined. As well as an ongoing contribution rate in respect of current employees, the Council also has

pension liabilities in respect of some former employees which it discharges through what we term the 'deficit back-funding lump sum'. That deficit lump sum is discharged (subject to valuation movements) over a period of time as advised by the actuary – and I am hopeful that the actuary will confirm that the term will end during the lifetime of this MTFS. If this is the case this is one less liability the Council will need to carry in its medium term financial plans.

- 1.4.6 The current valuation is taking place and we will hear in the next few weeks and months what the new contribution rates for employers' pension contributions will be from April 2023 onwards. Given the recent turbulence in the financial markets following the mini-budget on 23 September, the potential outcome of this valuation is especially difficult to predict at this time.
- 1.4.7 Nevertheless, a further update of the MTFS has been prepared which Members need to view as '**work in progress**' and clearly is sensitive to movement in any of the factors listed. As there becomes more certainty about some of the factors above, the MTFS will be updated again but **for NOW** our calculations suggest that (based on best information to date) **the funding gap could lie anywhere between £2.6m at best case to £3.8m at worst case.**
- 1.4.8 Members will of course wish to understand why there is such a divergence in these figures. Put simply, this is connected to the level of certainty (or in most cases, uncertainty) we have about key factors within our MTFS. The following gives Members a 'flavour' of this.

*Settlement Funding, Negative RSG and New Homes Bonus*

- 1.4.9 Recent change to national leadership has thrown into question whether there will be a Spending Review in the coming months for local authority funding, or whether the government will rely on previous years data. Previous year data did not allow for the effects of surging inflation that is currently affecting all aspects of the economy. The indications are that whatever happens we may only receive a settlement for one year, which does not aid financial planning.
- 1.4.10 The Fair Funding Review does seem to have been put back once more following the appointment of a new Secretary of State. It was our view that the issue hanging over TMBC (and similar councils) of "Negative RSG" would be resolved one way or another within a Fair Funding Review – and the outcome of such a review would be very unlikely to favour councils like TMBC. Therefore, deferring the Fair Funding Review in some respects is advantageous – but it will only be a matter of time before it does happen and whilst we can benefit from a short term "windfall", in the longer term we must prepare for a much harsher reality. Cabinet is reminded that the assumed value of "Negative RSG" is around £1m and we have for modelling purposes assumed it will be reflected in our settlements from 2024/25.

1.4.11 In terms of New Homes Bonus, the government consulted local authorities back in March 2021 regarding the future of the scheme (with the inference being that it would cease) but nothing further has been announced since. The scheme has in recent years been diluted, but if it continues in some form or another for a while longer, this provides a level of income (assumed as £600,000) that can be reflected in our financial plans.

*Business Rates Retention and Pooling*

1.4.12 The Council has been on or around its baseline for business rates retention over the last year or two, but with the imminent launch of the Panattoni site on the former Aylesford Newsprint premises, the opportunity to generate more business rates for our community is presented.

1.4.13 As Cabinet will know from my report to Council on 25 October, partners in the Kent Business Rates Pool have invited TMBC to re-join the pool from April 2023, subject to approval from the Secretary of State.

1.4.14 If the approval is given, this opens up the opportunity to retain a greater proportion of the business rates that are generated (at least for a yet to be defined period). Until we hear from the Secretary of State (likely to be December), it is not known whether we can (or can't) assume retention of a greater proportion of the business rates.

*Pension Fund Triennial Revaluation*

1.4.15 As mentioned earlier at paragraph 1.4.5, the triennial revaluation is awaited. Not only will this determine the ongoing contribution rates in respect of the current employee base, it should also shed light on whether (or not) we can formally "discharge" the liability in respect of the deficit lump-sum during the lifetime of this MTFS or whether the period of liability is extended.

1.4.16 At this point it is hard to predict whether contribution rates will go up or remain stable (especially given the current turmoil in the markets); and/or whether the deficit liability will be either discharged or extended.

*Council Tax Increases*

1.4.17 We will not know until closer to the time of budget setting in February, what 'parameters' the Secretary of State will impose in respect of council tax increases.

1.4.18 For now, our assumption is that council tax could be increased by £5 (at Band D). This represents only a 2.2% increase on the previous year, which is below inflation. Naturally we will need to update this as and when more information comes to light.

1.4.19 It is worth noting that **IF**, in light of current inflation, the Secretary of State were to relax the threshold for council tax increases for district councils to say £10

(mirroring the limit that has been afforded to Police authorities) for the year 2023/24 only, this could have the effect of reducing the funding gap, potentially by up to £0.5m if this can run in parallel with the effect of the cessation of the pension fund deficit. Members should note that this has not been modelled into any of our scenarios and there is no suggestion at this time that it might be an option that could be put forward by the Secretary of State. Nevertheless, it is worth reflecting on this point given the impact this could have.

*Inflation, Energy Prices and Investment returns*

- 1.4.20 In preparing estimates for the 2023/24 budget I have advised Services that they should assume 10.1% for CPI and 12.3% for RPI, and 15% in respect of the Waste contract.
- 1.4.21 As I said earlier, latest advice from the Bank of England is that inflation is expected to peak at 11% for CPI. The September figures recently published show CPI at 10.1%.
- 1.4.22 Our largest contract – the Waste contract – is annually uplifted based on an amalgam of RPI and diesel indices as at October. When preparing the MTFS back in February, we assumed a 4% increase in the Waste contract from April 2023 – but with surging inflation we are now modelling 15% which adds circa £450,000 to the funding gap. Each 1% gives a variation of around £40,000, and given the turmoil there has been in the economy, we will not have any certainty until the relevant indices are published.
- 1.4.23 Government have announced assistance in respect of energy costs to businesses and public sector bodies. However, the detail of that has not yet filtered through. The greatest energy cost the Council bears, under certain circumstances, is in relation to support for the leisure centres which are in the Council's ownership but are managed by the Tonbridge and Malling Leisure Trust. Irrespective of the government support the payment this year could be in the order of £650,000 with a further payment in future years dependent on where energy prices are at the time and the trading performance of the Trust.
- 1.4.24 The Council is of course benefiting from the increase in interest rates through its investment portfolio. However, the MTFS had already assumed a steady rise in rates towards the latter years, and therefore this 'earlier than expected' rise is simply acting as a "windfall".

*Reassignment of other reserves and balances*

- 1.4.25 Members will see that it has been exceptionally difficult at this time, given all the uncertainty, to formulate firm updates to our MTFS.
- 1.4.26 One further suggestion my team and I bring forward is to review the level of reserves and balances we hold for other specified purposes and add them back into the general revenue reserve if required or deemed appropriate.

- 1.4.27 Why does this help? As set out in paragraph 1.2.3, the MTFs is founded on a number of objectives. There are two important objectives here which need to be met at the end of the 10 year strategy period to ensure the Council has financial sustainability - one of those is to ensure there is a balanced budget, and the other is to retain a balance of £3.0m in the General Revenue Reserve (GRR). The Council's stance has always been to utilise reserves to assist in the smoothing of savings so as to protect service delivery for as long as possible. Naturally therefore, reserves will be depleted over the 10 year MTFs period, and the "funding gap" scenarios we have identified take into account the fact that we need to protect the GRR balance at the end of the 10 year period so it does not drop below £3.0m.
- 1.4.28 If the GRR could be supplemented, it is therefore possible for us to re-model and potentially reduce the "funding gap". Members should note that because of the way the MTFs works there is not a £ for £ relationship, and it depends on how and when all other 'factors' interact with each other. Nevertheless we estimate that if we could, for example, release £1.5m from other reserves and balances and add those funds to GRR, this could reduce the funding gap. This is worth exploring but it does mean that funds would need to be released that are set aside for other specified purposes. I would recommend that Cabinet request Management Team to undertake this work, and I have reflected the impact of doing so in the "best case" scenario that I set out at paragraph 1.4.7.

#### *Summary*

- 1.4.29 Members and senior officers have a duty to provide for the long term financial sustainability of the Council. Therefore whilst we hope the worst case scenario does not materialise we, at least, need to prepare ideas as to how to respond to it.
- 1.4.30 Notwithstanding that, it is imperative that we prepare plans to deliver any scenario (best, middle or worst). Dividing the funding gap into tranches as we have done for many years allows us to "flex" the approach as new information comes forward.
- 1.4.31 Our assessment is that we need to escalate plans to deliver savings of £1.5m within the next 3 years, inclusive of the tranche of savings (see 1.5 below) that is already in train. In outline that might mean:

Tranche 1 – underway £350,000 – by April 2023

Tranche 2 – £500,000 – by April 2024

Tranche 3 – £650,000 – by April 2025

Cabinet will of course appreciate that there would be other Tranches to follow, with levels dependent upon whether we are at the "best" or "worst" case funding gap level (see paragraph 1.4.7).

## 1.5 Savings Identified

- 1.5.1 As mentioned earlier at paragraph 1.1.4 at its meeting in June Cabinet resolved that *"in order to ensure that the target of £350,000 is achieved by the start of the financial year 2023/24, a comprehensive report detailing all strands of work being undertaken in respect of the Savings and Transformation Strategy, including progress being made on achieving targets and outcomes be presented to Cabinet in November 2022"*.
- 1.5.2 Savings that have been identified thus far have been reported by the 'Financial Planning & Control' report, initially to Cabinet and latterly to the Finance, Regeneration and Property Scrutiny Select Committee.
- 1.5.3 The savings can be summarised as follows:

	£
Grants to Voluntary Groups	1,600
Members Allowances (no increase)	8,150
Replacement of Uniform System	50,000
Cleaner Borough Co-ordinator	18,800
Housing Technical Officer	750
Insurance	60,000
Out of hours service	15,000
Events Income	10,000
<b>Total (to date)</b>	<b>164,300</b>

- 1.5.4 As Members will see from the table above, there is still some way to go in order to achieve the £350,000 tranche 1 target. Work continues to identify savings options ahead of 1 April 2023, including the examination of the levels of fees and charges levied for council services. Members are referred to the report of the Management Team elsewhere on this agenda in respect of "Fees and Charges".
- 1.5.5 It should also be remembered that this does not take into account costs that have taken the funding gap in the wrong direction, some of which could be outside of the Council's control.
- 1.5.6 Of course, this is only addressing the first tranche of a much bigger funding gap as outlined in section 1.4. **In terms of tranches 2 onwards, urgent and**

**concerted effort will need to be made by both Members and officers in identifying how these significant sums can be found.** This undoubtedly will be a combination of “big ticket items”, service rationalisation, cessation of services with least priority, and the continued search for efficiencies. **Only this will ensure the continued financial sustainability of the Council.**

## 1.6 Legal Implications

- 1.6.1 Section 151 of the Local Government Act 1972 requires every local authority to make arrangements for the proper administration of their financial affairs and requires one officer to be nominated to take responsibility for the administration of those affairs.
- 1.6.2 Section 114 of the Local Government Finance Act 1988 requires a council’s chief finance officer to issue a s114 Notice reporting to all elected members an actual or impending seriously unbalanced budget.

## 1.7 Financial and Value for Money Considerations

- 1.7.1 The Council maintains a prudent level of reserves to provide a safety net for unforeseen or other circumstances. The Robustness of Estimates and Adequacy of Reserves statement that the Council’s Chief Financial Officer (i.e. myself as Director of Finance & Transformation) is required to produce under the local Government Finance Act 2003 to support Members in considering the Budget Setting report, lists examples of why the Council needs to retain a minimum level of reserves. Examples include Emergencies; Economic and world recession; Interest Rate volatility; Income volatility; and Government Legislation. Rather than one or even two of these examples occurring, we have the situation of all of these examples impacting at the same time.
- 1.7.2 The Council has resolved to hold a minimum level of general revenue reserve of £3 million in order to provide for a host of potential financial and operational risks. At the start of 2022/23, the general revenue reserve balance was circa £7.7m and together with the budget stabilisation reserve giving some headroom to deal with issues arising without more immediate ‘draconian’ measures.
- 1.7.3 Significant savings are required by April 2028 in order to preserve the integrity of our financial plans. These are **extremely** challenging times, and it has never been more important than to now focus firmly on the delivery of the necessary savings.

## 1.8 Risk Assessment

- 1.8.1 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 and in the current climate regularly reviewed by Management Team. In

addition, not identifying and implementing the requisite savings and transformation contributions will put at risk the integrity of the MTFS.

- 1.8.2 Through prudent husbandry of resources, Council has reserves, including a Budget Stabilisation reserve, to help to smooth the path in the delivery of savings. However, reserves are finite and it is imperative that actions are taken at the earliest opportunity in order to preserve the longer term financial sustainability of the Council.
- 1.8.3 Much debate has been made of the potential and (perhaps necessity in some cases) for local authorities to issue s114 notices (under the s114 (3) of the Local Government Finance Act 1988). For Members' information this says that the Chief Finance Officer of a relevant authority shall make a report under this section if it appears to him/her that the expenditure of the authority incurred (including expenditure it proposes to incur) in a financial year is likely to exceed the resources available to it to meet that expenditure. As Cabinet will have gathered, due to careful and prudent husbandry of resources in the past, I do not believe that TMBC is yet in this position. **However, it is imperative that we carefully monitor and contain expenditure and continuously update our forecasts to ensure that we remain on track.** This will of course include reflecting in our forecasting the outcome of the Fair Funding Review and Business Rates Reforms which is as yet an unknown quantity.
- 1.8.4 The financial position is recorded as RED on the Strategic Risk Register, and Cabinet's attention is drawn to this.

## 1.9 Equality Impact Assessment

- 1.9.1 Where there is a perceived impact on end users an equality impact assessment has been carried out and as further savings and transformation options emerge, further equality impact assessments will need to be carried out as appropriate

## 1.10 Policy Considerations

- 1.10.1 Budgetary and policy framework is relevant to all areas of the Council's business.

## 1.11 Recommendations

- 1.11.1 Cabinet is **RECOMMENDED** to:

- 1) Note the latest forecast of the Medium Term Financial Strategy and the funding gap which is now estimated to be in the range £2.6m at best case to £3.8m at worst case (see paragraph 1.4.7).
- 2) Note the savings/transformation contributions for Tranche 1 totalling £164,300 as set out in paragraph 1.5.3 and consider how the balance of £185,700 savings can be found.

- 3) Consider how a programme for investigating and identifying the necessary savings for tranches 2 onwards can be implemented and actioned as soon as possible.
- 4) For the reasons set out in paragraphs 1.4.27 and 1.4.28, request that Management Team review the level of reserves and balances held for specified purposes in order to release any 'surplus' sums to the General Revenue Reserve.

Background papers:

Nil

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