

ITEM

ITEM

Executive – 8 September 2005

MEDIUM TERM RESOURCE STRATEGY 2006/07 TO 2010/11

Report of the Head of Financial Services

Statutory Powers: Local Government Act 1972, Section 151

Financial Implications: This report identifies the potential budget gaps for the five years to 2010/11.

Purpose

To provide an updated forecast of the financial situation for the five year period to 2010/11. The forecast is intended to provide a framework within which decisions can be made regarding future service provision and council tax levels. The consideration of this issue is directly linked to CP6 – the improvement of core services in a cost effective way.

RECOMMENDATION

That the Executive RESOLVES that the report be noted.

Introduction

- 1 Members will be aware of the intense pressure exerted by Government on local authorities to keep council tax increases down with a number of councils being capped this year. The Government have yet to make any formal announcements concerning council tax rises for next year but it is likely that they will require them to be in low single figures.
- 2 It is therefore essential that we continue to set our annual budget within the context of a rolling five year resource strategy. A longer term strategic view must be taken when decisions are made that have a financial impact beyond the annual budget as it enables us to assess the sustainability of decisions. The strategy is linked to our key strategic objectives and incorporates both national and local improvement priorities which have been included in our individual service plans and strategies.
- 3 This report contains the following sections to assist in understanding and interpreting the strategy:

Section A explains the key general economic assumptions together with factors specifically relating to South Hams.

Section B provides further explanation of the budget pressures faced by the Council.

Section C provides a summary of the overall position and describes the next steps in the budget process.

SECTION A - Key Assumptions and Available Resources

- 4 To be able to produce a meaningful resource plan a number of assumptions have to be made and regularly kept under review. Economic factors such as inflation and interest rates have a huge on our financial position. The main economic assumptions included within the strategy are as detailed in Appendix A.
- 5 **Revenue Support Grant (RSG)**- The Government's 2004 Comprehensive Spending Review set out the broad national spending plans until 2007/8. For 2006/07 it includes a 3.5% increase for the Environmental, Protective and Cultural Services (EPCS) block which covers most District Council's services. Unfortunately it does not go into enough detail to accurately forecast the Revenue Support Grant that an individual authority will receive, it just details spending by public policy areas. The position is further complicated because last year's final grant allocation included a 'one-off' amount to help keep council tax increases down. To date no announcement has been made if this will continue for future years.
- 6 The RSG figure in the our forecast for 2006/07 is based on an uplift in line with consumer price inflation of 2%. Provisional grant levels will not be announced by Government until November with final conformation in early 2006, which as always is very late in the budget cycle.
- 7 **Council Tax Property Revaluations** - These are due to take effect in April 2007. The effects on individuals and councils will not be known until later in 2006 but property values in the South Hams have risen considerably over the years and, importantly they are likely to have risen faster than the national average.
- 8 This is a very complicated subject and the Government have not decided how the impact of the revaluation will be dealt with across the country. They have announced that the whole exercise will not, in itself lead to an increase in council tax yield across the country. However, there is likely to be a large number of tax payers who will either pay more or less council tax depending upon how their property value has moved compared to the national average.
- 9 For individual taxpayers there could be a form of transitional relief which will spread any increase in tax over a period of time. The Government may also look at other measures such as regional tax bands. For local authorities the situation regarding their RSG is also very unclear.

- 10 A key factor in the distribution of RSG is the taxbase which is directly linked to the property values in the area. In broad terms the higher the taxbase the less RSG is received. A possible scenario is that we could have a nil increase in our budgeted net expenditure but be forced into levying a higher council tax purely because of the loss of RSG. As with the case for householders government may introduce a period of transition to cushion the full impact of any changes over a period of time.
- 11 As far as our strategy is concerned, it has been assumed that we will not get a cash increase in grant for 2007/08 and 2008/09. This is based on the assumption that property valued in our district have risen faster than the national average, hence we will get a smaller share of the RSG. This is very much a prudent, cautionary view as we have no indication of the overall impact of the revaluation.
- 12 **Council Tax Income** – Although Government have indicated that they want to keep council tax rises low, this is at odds with the implications for council tax in the Spending Review which planned for increases in tax of 6.7%,5.5%, 5.1% in 2005/06, 2006/07 and 2007/08 respectively.
- 13 However, the financial strategy has assumed increases of 3% per annum as this is near the level of Retail Price Inflation and the level of our anticipated pay awards. If lower tax increases were required it would mean that for each 1% reduction in tax, additional savings of £42,000 would be required.

SECTION B – Budget pressures/reductions

- 14 Appendix B illustrates the financial impact of the budget pressures on the Council's financial position for 2006/07. The main considerations included in the forecast are as follows:
- 15 **Waste Review** – To comply with statutory recycling targets for household waste, the Council has already approved plans which will increase the net cost of the service by £66,000 per annum in 2006/07.
- 16 **Interest on Investments** – On 31st March 2005 we paid the Devon County Council Pension Fund a capital sum of £7.5m to maintain our pension contributions at the current level. This together with lower interest rates and using capital receipts and reserves to finance our capital programme results in a declining level of investment interest.
- 17 In overall terms the decision to make a capital pension payment will save us £200,000 per annum from 2007/08, the first full year of what would have been the proposed increase in pension contributions.
- 18 **Leisure Centres** – For the purposes of the budget strategy it has been assumed that the proposed transfer of the facilities will take place in October 2006.

- 19 **Single Status** – The term Single Status is used to describe the harmonisation of pay and conditions for all of our employees. All local authorities have to complete the review by 31st March 2007. It covers a wide range of issues including pay grades, productivity, flexible and variable working arrangements, training and learning.
- 20 Whilst we have legal obligations to proceed with the review it also provides an exceptional opportunity to modernise our pay structures, which will provide opportunities to facilitate increased staff flexibility and motivation. This will be one of the key features for the proposal to explore ‘Blue Sky’ new ways of working which has been approved by the Executive. In addition there is also evidence now available that providing staff with more flexible working reduces sickness absenteeism and improves services provided to the public.
- 21 Experience from other local authorities who have completed their reviews indicates that it may cost in the region of £400,000. This is primarily a result of old CCT type contracts where staff were employed with less beneficial terms and conditions. These contracts have now ended and staff will have the normal terms and conditions reinstated under the review. However, the budget projection shows savings of £1m over the period to 2010/11 which will be partly facilitated by flexibility and productivity gains arising from Single Status.
- 22 **Triennial Pension Revaluation** – The next revaluation is due in 2008 and a sum of £200,000 has been included for 2008/09. This is a very rough figure and based on the effect of the Government’s decision to revoke the changes which were included in the last revaluation (reductions in employee benefits). The actual amount will depend on a large number of factors that happen before 2008 including, inflation, interest rates, investment returns, life expectancy and changes to the benefits of the scheme. There is a possibility that following the Government’s decision to revoke the changes local authorities will have to undertake a revaluation by next March. We will not know this until later in the year and the situation will be kept under review. It may be wise to make provision in our budget forecast for an ongoing or one off contribution from 2006/07 to offset or prepare for future needs.
- 23 **Inflation** – The estimated cost of inflation, net of inflationary increases in charges is £306,000 for 2006/07.
- 24 The impact of the budget pressures, increased RSG and council tax when added to the base budget from 2005/06 is shown in Table 1:

Table 1. Calculation of the Initial Budget Gap

	2006/07 £000	2007/08 £000	2008/09 £000	2009/10 £000	2010/11 £000
Base budget brought forward	8,857	9,395	10,029	10,699	11,222
Inflation and budget pressures	538	634	670	523	446
Total expenditure	9,395	10,029	10,699	11,222	11,668
Government Grant	4,686	4,686	4,686	4,780	4,876
Assumed 3% council tax increase	4,374	4,523	4,678	4,838	5,003
Surplus on Collection Fund	34	34	34	34	34
Total income	9,094	9,243	9,398	9,652	9,913
Budget gap per annum	301	786	1,301	1,570	1,755

Options to close the budget gap

- 25 Table 1 clearly demonstrates that without serious management the future budget is not sustainable. A number of options have therefore been considered to close the budget gaps. These are summarised in Appendix C and discussed below.
- 26 **Efficiency ‘Gershon’ targets** – Efficiency is not about cuts, but about raising productivity and enhancing value for money.
- Reducing inputs (money, people or assets) for the same outputs
 - Reducing prices (procurement, labour etc.) for the same outputs
 - Getting greater outputs or improved quality (extra service, productivity) for the same inputs
 - Getting more outputs or improved quality in return for an increase in resources that is proportionately less than the increase in outputs or quality
- 27 We are required to achieve a £320,000 (2.5%) efficiency target set by Government. Whilst only half of this is required to be cashable (as opposed to non cashable – providing more service for the same cost), to help balance the budget most of our efficiency savings will be cashable.
- 28 Heads of Service have therefore each been given efficiency targets to achieve for next year amounting in total to £250,000. In addition, a target of £50,000 has been set for efficiencies arising from procurement and productive time reviews. CMT have also been requested to identify any other budget reductions which could be considered for approval, it is important that budgets are continuously reviewed to ensure that they are still appropriate.
- 29 **Use of Reserves** - From next year it is proposed to cease paying interest into our reserves except for specific vehicle and plant replacements (to maintain the real value of money to buy the new vehicle). The level and commitments for each reserve are kept under

review each year and in future budget cycles it is intended to recommend specific payments into them to ensure they are adequate for the purpose for which they were established.

- 30 We also have a Building Control reserve comprising surpluses of £165,000 made in earlier years. Previous guidance stipulated that this money should be ring fenced and could not be used for general expenditure. However, we have now received written guidance to the contrary and propose to release £55,000 per year for three years into the General Fund accounts.
- 31 **‘Blue Sky’ new ways of working** – The July Executive approved a proposal to explore new ways of providing our services to the public. Although it is too early to predict which services will be changing or any financial implications, it is considered appropriate to include savings of £50,000 per annum from 2007/08, increasing to £75,000 in 2009/10.
- 32 **Local Authority Business Growth Incentive Scheme** - Under the scheme councils will receive a share of the annual growth in business rates in their areas. The scheme is very technically complex in it's administration but councils will receive a proportion of increases in local business rate revenues to spend on their own priorities. The exact amount will not be known until the end of each financial year but a prudent sum of £50,000 has been assumed for each year.
- 33 The overall effect of the proposed options to close the budget deficit identified in Table 1 in shown below:

Table 2. Options to close the Budget gap

	2006/07 £000	2007/08 £000	2008/09 £000	2009/10 £000	2010/11 £000
Budget gap from Table 1	301	786	1,301	1,570	1,755
Cumulative Total of the options (Appendix C)	(430)	(935)	(1,240)	(1,390)	(1,540)
Revised budget gap (surplus) per year	(129)	(149)	61	180	215

- 34 The budget surplus shown in Table 2 for 2006/07 arises largely due to the efficiency targets included in the budget assumptions and it is considered appropriate to redirect £100,000 of these savings towards our key priorities. This will continue the policy from previous years of redirecting resources to facilitate a continuous improvement in our services to the public.
- 35 It is proposed to invite bids that demonstrate an improvement in our key priorities or are seen as critical to the maintenance of the service.

- 36 Using £100,000 in this way will still leave a small amount of headroom for next year but will have the effect of increasing the budget gap in future years. Whilst this is of some concern it is considered that future assumptions and targets for Single Status, efficiency savings and 'Blue Sky' ways of working can be revised in the light of experience. It is important that we continue to redirect resources to improve key service priorities otherwise we are in danger of standing still as a council.

Pressures not yet built into the forecast

- 37 **Concessionary bus fares** - In his 2005 budget speech, the Chancellor announced that free off-peak local bus travel, rather than the current half-fare arrangement, would be provided for disabled people and those aged 60 and over. The new arrangements take effect from April 2006 and the Government will increase funding to local authorities by £350M per year from 2006/07, to meet the additional costs.
- 38 A final decision has not yet been made how the extra funding will be allocated to authorities but there is a risk that not all costs will be covered due to the way grants might be calculated, especially if it distributed through RSG. Consultations are currently taking place at national level regarding the exact calculations to be used. We are a member of the Devonwide Concessionary Fares Partnership which has carried out considerable research into the issue and has lobbied Government to protect the interests of the Councils in Devon. The situation will be kept under review and reported as soon as any firm information is received.
- 39 **Land Charge Search Fees** – The Constitutional Reform Act 2005 includes provision which could materially affect the level of Land Charge search fees which local authorities can charge. At present, certainly in Devon, authorities make substantial surpluses on their Land Charge Service, ours is £180,000 which ultimately help towards keeping the council tax down.
- 40 Proposals contained within the Act could force local authorities to set the charges at a level to merely recover costs. Discussions are taking place between Government officials, LGA, SOLACE and the Office of Fair Trading with regard to the new regulations and when they will come into force. The situation will be kept under review and reported as soon as any firm information is received.
- 41 **Sherford Community** – At this stage it is not possible to estimate either the timing or additional cost of the services that the development will require. New housing will generate additional council tax income to help fund related services but there will be a considerable time lag between development of services and recovery from council tax. However, it is important that this be kept under review and services plan as early as possible for the impact of the scheme.

SECTION C – Summary, Next Steps and Conclusion

Summary

- 42 The following table summarises the budget forecast included in Appendix D for the forthcoming five years. It shows the budget gap after taking into account the redirection of £100,000 towards key priorities in 2006/07 and future council tax increases of 3%.

Table 3 : Summary of the 'Budget Gap'

	2006/07	2007/08	2008/09	2009/10	2010/11
	£000	£000	£000	£000	£000
Estimated expenditure	9,065	9,194	9,559	9,932	10,228
Projected available resources	9,094	9,243	9,398	9,652	9,913
The budget gap	(29)	(49)	161	280	315

- 43 There is a requirement to achieve substantial efficiency savings in order to finance the inescapable service pressures included in the forecast. This is a fundamental requirement before any new bids for priority service improvements can be.

Next Steps

- 44 The following paragraphs set out the next steps in this year's budget process.
- 45 **Service bids** – Details of service bids should be invited which demonstrate an improvement in our key priorities or are seen to be critical to the maintenance of the service.
- 46 **Efficiency savings and budget reductions** – Details of efficiency savings and reductions are currently being gathered together for Members consideration and prioritisation in terms of the funding gap identified above. This process will enable Members to switch funds between competing demands and to refocus existing resources on key priorities.
- 47 **Fees and Charges** – Further increases to our major charges can be considered in terms of the overall budget strategy. In addition, Government are encouraging local authorities to examine the possibility of widening the scope of charging for services.
- 48 **Benchmarking comparisons** – As in previous years, we will be making broad comparisons of South Hams expenditure with similar authorities. This will enable us to investigate whether expenditure is reasonable and

in accordance with corporate priorities raising questions where necessary.

- 49 **Balances and Reserves** - The decision on the level of balances and reserves is one of several to be taken during the formulation of next year's budget and the medium term financial strategy. Reserves are built up to meet anticipated future requirements and their investment earns approximately £42,000 for every £1m held. However, it is important to recognise other opportunity costs of holding reserves and ensure that they help meet our key priorities.
- 50 The budget and medium term financial strategy are based on forecasts of inflation, pay awards, Government funding, interest rates and the level of services to be provided. The existence of balances provides for the unexpected, including changes to these forecasts. The provision of an appropriate level of balances is a fundamental part of prudent financial management. The existence of specific reserves allows the Council to meet known future financial commitments such as the replacement of refuse vehicles or items of plant.
- 51 **Medium Term Resource Strategy assumptions** – These will be kept under review over the coming months and any new information regarding interest rates, grant, inflation etc. will be amended in the forecast.
- 52 **Capital Programme** – As part of the medium term financial strategy it will also be necessary to review the level and phasing of schemes within the capital programme. It is important that the programme is matched with available resources and the impact on reserves and the revenue budget fully assessed.

53 Risk Assessment

Risk	Mitigation
Failure of Council to set lawful budget	The Budget is compiled in accordance with best practice guidelines issued by CIPFA and the ODPM . The final budget report includes an assessment from the Section 151 Officer on the adequacy of the Council's reserves and the robustness of the estimates made for the purpose the budget calculations. The budget process is laid down in the Council's Constitution. Executive and Council meetings are timetabled to meet the Statutory deadlines for setting the Council Tax.
Failing to target budgets to service priorities	The Council prepares a Medium Term Financial Strategy covering a five year period. The strategy provides a framework within which decisions can be made regarding future service provision and council tax levels. All budget bids and reductions include a section on their impact on council priorities and a risk assessment. The budget is subjected to extensive consultation with all Members, the public, business community and Parish and Town Councils.
Failure to maintain a comprehensive budgetary control review system. Including monitoring of material items of income and expenditure.	Adequate levels of appropriately trained staff. Thorough planning and monthly monitoring of performance to management, quarterly to the Executive.
The financial strategy is based on a number of assumptions which include: Inflation rates, interest rates, the level of Government grant received, the level of unavoidable budget pressures facing the Council, and the result of the actuarial review of the pension fund.	Adopting a prudent approach to financial forecasting which involves obtaining information from external professional sources. Continuous monitoring and review of the key factors which involves regular reports to Members on any major issues.

Conclusion

- 54 This report updates the Executive with the latest budget forecast and explains the main budget pressures facing us. Formal consideration and review of the medium term financial strategy will ensure that decisions

are made in the correct context and provide Members with an opportunity to consider and challenge some of the key assumptions identified.

- 55 The Council has set out its' key priorities for the medium term and last year's budget clearly reflected those priorities. This forecast will provide the financial framework necessary for the consideration of service delivery and financing issues. The objectives of this year's process are:
- To continue to seek efficiency savings
 - The continuing redirection of resources to key priorities
 - To ascertain an appropriate and sustainable level of council tax
 - To determine the appropriate level of fees and charges
 - Be the starting point for consultation with the community, other council bodies and partners
- 56 This is the first of a number of reports the Executive will receive on the budget for 2006/07 and represents the start of the process. The coming months will involve much hard work and some difficult decisions for Members as they attempt to balance the resource needs of priority issues, meet mandatory service pressures and produce a sustainable budget for the forthcoming year.

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Executive
8 September 2005

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Background documents:
None