

PERFORMANCE AND GOVERNANCE COMMITTEE – 15 NOVEMBER 2011

FINANCIAL PROSPECTS AND BUDGET STRATEGY 2012/13 AND BEYOND

Report of the: Deputy Chief Executive and Corporate Resources Director

Also considered by: Cabinet – 13 October 2011

Status: For Decision

Key Decision: No

Executive Summary: The role of this Committee is to consider the development of the Council's budget strategy.

This report sets out the major financial pressures the Council is likely to face over the next four years, together with a proposed strategy for setting a balanced and sustainable budget for 2012/13 and beyond. The Council has an excellent track record in identifying, planning for and addressing financial challenges. In light of the challenging financial position facing all authorities a year ago, for 2011/12 the Council brought its budget setting process forward by two months and produced a 10-year budget together with a four-year savings plan. This provides the Council with a stable basis for future years, which addresses the reduction in Government funding as well reducing its reliance on reserves.

Building on the considerable progress made over recent years, this report updates Members on significant risk areas as well as setting out the way forward for service prioritisation, business and financial planning, financial strategy and the budget setting process.

The overall emphasis is on building on the strong framework provided by the 10-year budget, whilst taking into account any new financial burdens and changes in the economy that have an impact on budget assumptions. This report also provides Members with the proposed timetable for the budget setting process.

This report supports the Key Aim of effective management of Council resources

Portfolio Holder Cllr. Ramsay

Head of Service Head of Finance and Human Resources – Tricia Marshall

Recommendation:

That Members consider the attached report and feedback to Cabinet any comments on the proposed budget strategy.

Introduction

- 1 The Council's financial strategy over the past seven years has worked towards increasing financial sustainability and it has been successful through the use of a number of strategies including:
 - implementing efficiency initiatives;
 - significantly reducing the back office function;
 - improved value for money;
 - maximising external income; and
 - the movement of resources away from low priority services.
- 2 Over this period the Council has focused on delivering high quality services based on Members' priorities and consultation with residents and stakeholders through the Community Plan. In financial terms, the adoption of this strategy has to date allowed the Council to move away from its reliance on general fund reserves which has ensured that the general fund reserves have remained largely unchanged.
- 3 In setting its budget for 2011/12 onwards, the Council recognised the need to address both the short-term reduction in Government funding as well as the longer term need to reduce its reliance on reserves. The outcome was a 10-year budget, together with a four-year savings plan, that ensured the Council's finances were placed on a stable footing but that also allowed for flexibility between budget years.
- 4 The intention of this report is to enable Members to give early consideration to the pressures likely to be faced by the Council and put in place a long term solution that ensures service reductions are minimised. This report sets out the high level approach and principles but a report to Cabinet on 8 December 2011 will provide the budget details along with analysis of the areas the Cabinet has requested officers to consider in assisting the balancing of the budget, as well as feedback from select committees on proposed service plans for 2012/13 onwards.

Financial Pressures 2012/13 to 2021/22

Overall Summary

- 5 In the medium term, the Council will have to progress its savings plan and maintain tight control over net expenditure in order to deliver its 10-year budget.
- 6 The potential to increase income levels over the next few years is very limited. In some cases the Government controls the level of increase and in other areas current economic conditions make it uncertain as to whether the Council will even achieve existing income budgets.

- 7 Looking at expenditure, inflation is running at 4.5% (CPI). This Council is expected to receive a reduction of 11% in revenue support grant in 2012/13 and further reductions are expected in future years.
- 8 The paragraphs below set out the position in more detail and assess the impact on the current Financial Plan.

Income

- 9 **Revenue Support Grant/Non-domestic rates** (£4.9m in 2011/12) – The Council will have received a 29% reduction over two years since 2010/11. Included in the grant is an element for floor damping, which is expected to be £22,000 in 2011/12; the Government could decide to remove this protection. The Government is currently carrying out several consultations which are likely to have a significant impact on from funding stream from 2013/14 onwards. Each one percent reduction in grant would result in an income loss of £49,000. **Likely impact: unknown at this stage for 2013/14 onwards, but likely to have a serious impact on the Council's budget.**
- 10 **Council Tax** (£9.2m) – The financial plan assumes that there will continue to be a Council Tax freeze in 2012/13. Government capping may continue to limit future increases. 1% change equals £92,000. In the longer term, the localisation of and 10% reduction in council tax support (previously council tax benefit) could have an adverse effect on collection rates. **Likely impact: unknown at this stage.**
- 11 **Investment income** (£0.2m) – returns are continuing to fall due to low interest rates and the revision of the Council's current Investment Strategy towards a low risk approach. It is certain that the Council's reserves will continue to fall due to their use in the 10 Year Budget, so as a consequence, investment income will continue to reduce. The latest assumption is for the following returns: 0.9% in 2012/13, 1.7% in 2013/14, 2.7% in 2014/15 and 2.8% in later years. **Likely impact: nil taking into account the level of balances forecast.**
- 12 **Landsbanki** – efforts are continuing to recover the £1m invested in Landsbanki in June 2007. An impairment adjustment for the potential loss has been included in the 2008/09 accounts. **Likely impact: minimal in future years if 95% is recovered apart from loss of interest until the money is received.**
- 13 **Variable income sources** – The Council receives income in fees and charges from a number of sources. This includes (income figures are shown gross):
- Land Charges (£0.2m);
 - Development Control (£0.6m);
 - Building Control (£0.5m); and
 - Car parks (£2.0m);

- On-street parking (£0.7m).
- 14 The first three are linked to some extent to activity in the housing market and remain vulnerable, with some adverse variances against budget in the current year. **Likely impact: no change but with a risk of shortfalls in these income areas.**
- 15 Despite the current economic conditions car park income is at budgeted levels but on-street parking income is currently below budget. **Likely impact: no change at this stage but will be dependent on economic conditions .**
- 16 **External Funding** (£0.7m) - the Council has been very successful in securing external funding across a range of services, based on it delivering a wide range of innovative services, often in partnership with other agencies, to local residents. The Council's officers continue to seek new opportunities for funding. As financial constraints are put on public services the funding available from health and other public bodies is expected to reduce. **Likely impact: No financial impact but services currently externally funded may cease to be provided.**
- 17 **Discretionary Charging** This area is regularly reviewed and will be further developed when the Government finalises legislation in this area. The budget already assumes that in 2012/13 additional income of £150,000 will be generated from discretionary charging. **Likely impact: Unknown until the legislation is finalised.**
- 18 **Partnership working** - Various services have included savings from partnership working in recent years budgets and this continued to be an area that is being investigated. The Council successfully works in partnership with other authorities in a number of areas, including Environmental Health, Revenues, Benefits, Internal Audit and Anti Fraud, Licensing, Finance, Development Services and IT. A programme of more extensive partnership working with other authorities is being investigated to generate further efficiencies for the Council. **Likely impact: Savings based on shared services are already included in the four-year savings plan, so successful partnership working would secure these savings.**

Expenditure

- 19 **Pay** costs total £12.5m and form about half the Council's gross expenditure (excluding Benefits payments). The pay award for 2012/13 is expected to be 0% which will be the third year that there has been no increase. The Financial Plan assumes a pay increase of 1% in 2013/14, 1.5% in 2014/15 and 2% in later years. These percentages are below current inflation rates, though inflation is projected to fall. In the economy as a whole pay awards are running at just over two percent. Every one percent change equals £125,000. **Likely impact: none if current assumptions are retained.**
- 20 **Non-pay costs** – the budget assumes non-pay costs will increase by an average of 2.5% a year. In practice items such as rates and energy costs have risen at a higher rate, so other non-pay items have been allowed a much lower inflation increase. Inflation is currently at 4.5% . **Likely impact: none if**

overall non-pay inflation can be contained to 2.5%, though this is viewed as challenging to achieve.

- 21 ***Unavoidable service pressures*** - One of the lessons to be learnt from previous financial strategies is that there is always a likelihood of unavoidable service pressures and there needs to be a clear strategy in dealing with these. The model does not allow for unavoidable service pressures, therefore these will need to be met from within existing budgets. These have not yet been identified to be included in the revised Plan, but they could be significant.
- 22 Based on previous experience, growth items totalling up to £0.5m a year could occur although, having the 4-year savings plan and the 10-year budget in place is likely the figure will be less than £200,000. Officers are still identifying the likely service pressures for 2012/13, particularly in relation to external income. These will be presented to Members as part of the Service and Performance Plans process. ***Likely Impact: In the region of £200,000.***
- 23 ***Progress on current ten-year budget*** – 2012/13 will be the second year of using the 10 year budget. The savings plan includes 63 items and some of those contain a significant element of risk. Together with Portfolio Holders, Management Team and Heads of Service are closely monitoring progress in delivering the savings, but it is inevitable that some savings will either be delayed or not achieved. The main risk items are those which rely on third parties or the generation of additional income. The latest version of the 10-year budget is set out in Appendix B. ***Likely impact: TBA***

Proposed Business and Financial Planning Strategy

- 24 In order to maintain a viable Council that continues to deliver on its main priorities and the services it provides to its residents, it is proposed that a Financial Strategy that embraces the following principles continues to be adopted:
- A ten-year balanced budget;
 - Flexible use of the Budget Stabilisation Reserve;
 - More effective use of remaining earmarked reserves;
 - Structured use of capital receipts;
 - The review and tighter management of inflationary pressures; and
 - A streamlined Service and Financial Planning process.

A ten-year budget

- 25 Five years ago, the Council adopted a ten-year financial model and following the recommendation by the Audit Commission, other councils have now put in place similar approaches. A ten-year budget was compiled for the first time last year. This required the Council in broad terms to extend its four-year financial planning and budget setting to ten years with the key requirement

being that over the ten-year period, although there will be fluctuations, the overall budget would be balanced.

- 26 Our external auditor made the following comment in the Value for Money section of his Annual Governance Report 2010/11. “Sevenoaks District Council has strong financial governance. Financial planning is robust and forward looking. With these sound arrangements for financial control it is well placed to maintain a secure and stable financial position. The Council has an established financial planning process with a 10 year budget. This allowed it to identify the budget gap and conduct early modelling over a range of scenarios. The Council’s 2011/12 budget was the earliest within Kent.”
- 27 Financial uncertainty has increased in recent years and this approach also enables the Council to more effectively deal with peaks and troughs in its financial position, thus increasing its financial resilience.

Flexible use of the Budget Stabilisation Reserve

- 28 The figures in the 10 Year Budget are based on a number of estimates and assumptions and are subject to considerable uncertainty in later years. The Budget Stabilisation Reserve provides Members with a mechanism for smoothing unexpected movements between budget years. However, this still requires a structured budget-setting process to ensure an annual balanced budget.

More effective use of earmarked reserves

- 29 At 31 March 2011 there was £6.9m of reserves allocated to asset maintenance and the pension fund deficit. It has been agreed that, allowing for an emergency asset maintenance reserve of £1m, the remaining £5.9m be used over the ten-year period equally to smooth the rundown of these reserves.
- 30 This still means that the Council relies on its reserves, however, the level of reliance has significantly reduced from almost £2m to £590,000 per annum. In the longer term, more sustainable solutions could be sought and if the economic recovery results in positive outcomes for the Council then the reliance on this reserve can be reduced or its period extended beyond the ten years.

Structured use of capital receipts

- 31 Up until 2010/11, the Council used its capital receipts to fund its capital programme. However, due to a combination of reducing assets and a period of recession impacting asset values, the level of historical reliance on capital receipts could not be sustained. Therefore, Members made the decision to fund the capital programme through the revenue budget. However, there are a number of potential capital receipts that the Council is likely to receive in the coming years and £1m has been ‘top-sliced’ from these receipts and equally spread over the ten-year budget programme period. This allows the capital programme to receive some realistic, predictable and long-term funding

The review and tighter management of inflationary pressures

- 32 In recent years, and for the future, one of the most significant challenges the Council has faced is, that whilst its income is reducing and its expenditure is being matched to this reduction, the gap between income and expenditure widened due to inflation. The inflation assumptions have been tightened accordingly. However, this will continue to be dependent on a number of factors, including national pay settlements, changes to staff terms and conditions, economic inflation levels and the Council's ability to generate extra income.

Streamlined Service and Financial Planning process

- 33 As part of the budget process, select committees will have the opportunity to comment on and challenge service plans and the Council's prioritisation matrix before their consideration by the Cabinet. This ensures that the Council's priorities and key service objectives drive the allocation of resources within its budget.

Process and timetable

- 34 Members will note from the timetable set out in the appendix that this report will also be considered by the Performance and Governance Committee at its meeting on 15 November 2011 and any comments will be considered by Cabinet at its meeting on 8 December 2011. It is proposed that Cabinet will agree its draft budget on 8 December 2011 along with its proposed areas for savings, Cabinet will agree its final budget on 9 February 2012 and full Council will consider the budget on 21 February 2012.

Consultation

- 35 In consultation with the Portfolio Holder, officers are in the process of agreeing a consultation strategy for the budget albeit that it will be limited as the Council has a 10-year budget in place.

Key Implications

Financial

- 36 All financial implications are covered elsewhere in this report.

Community Impact and Outcomes

- 37 Members' early consideration of the issues raised in this report would be beneficial to residents in that a planned approach to achieving a balanced budget should produce the best outcome for the community in limiting the level in budget reductions.

Legal, Human Rights etc.

- 38 None.

Conclusions

- 39 There is no doubt that there are a number of risks associated with this approach, including significant cost pressures that may destabilise the ten-year budget. However, by adopting this approach, many of these will be predictable and more importantly, the Council will be better placed to react to such events. This solution also allows the Council a little more stability and sustainability in delivering its services and dealing with its finances.
- 40 The Strategic Financial and Business Planning process has ensured that the Council follows a logical and well considered process and approach in dealing with the many difficult financial challenges which it has faced. The 10 year budget has further improved this process and helped to ensure that the Council is well placed in dealing with its more immediate and longer-term financial challenges.
- 41 Looking at the medium term, although the Council has made considerable savings in previous years and already plans to make further savings over future years, it is likely that additional savings will be required to meet the expected pressures.
- 42 This budget process will once again be a major financial challenge for a Council that already provides value for money services to a high standard. In making budget proposals, Members will need to consider the impact on service quality and staff well-being, to ensure that these proposals lead to an achievable 10 year budget that supports the Council's aspirations for customer focussed services.

Risk Assessment Statement

- 43 An effective integrated policy and priority driven long term financial and business process is required for the Council to deliver on its priorities and maintain a sustainable budget. It is also essential that continuous improvements are identified and implemented in order to take account of the changing climate within which the Council operates and to meet the expectations of both Government and the public on the quality of service demanded from this Council.
- 44 The risks associated with the 10 year budget approach include uncertainty around the level of shortfall and the timing of key announcements such as future grant settlements. The risk will be mitigated by continuing to review assumptions and estimates and by updating Members throughout the process.

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