

Agenda Item: 5

Report to: Budget Panel
Date of meeting: 11th January 2011
Report of: Head of Strategic Finance
Title: Draft Revenue and Capital Estimates 2011/2015

1.0 SUMMARY

1.1 This report sets out all relevant factors to enable draft revenue and capital estimates to be approved for the period 2011/2015.

2.0 RECOMMENDATIONS

2.1 That Budget Panel consider all relevant factors and recommend to Cabinet (as appropriate):

- * recommended expenditure levels for the period 2011/2015
- * consideration regarding the use of reserves and balances
- * future levels of council tax
- * future strategies to meet efficiency savings

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3.0 INTRODUCTION

3.1 The preparation and finalisation of the Budget for 2011/2012 has been completed against a background of unprecedented reductions in Central Government funding to local authorities and progress in developing revenue and capital estimates has been regularly reported to Budget Panel at previous meetings.

3.2 The purpose of this report to Budget Panel is to provide all relevant information to enable recommendations to be made to Cabinet (17th January) regarding:

- recommended expenditure levels for the period 2011/2015
- consideration regarding the use of reserves and balances
- future levels of council tax
- future strategies to meet the exceptionally stringent public expenditure reductions

4.0 Central Government Draft Revenue Support (Formula) Grant Settlement

4.1 The Budget Panel, at its last meeting on 2nd December had limited information regarding the Governments RSG Settlement for Watford. This information was not available until 13th December and was considerably worse than could have reasonably been anticipated.

4.2 Detail of the draft Settlement was circulated to all members of the Council on 16th December after a few issues had been clarified. In essence the settlement for Watford reduced RSG Formula grant from £8.072m in 2010/2011 to £6.009m in 2011/2012 and £5.218m in 2012/2013. For the period 2013/2015 no firm figures have been provided and necessary assumptions have had to be made.

4.3 A summary of the draft settlement (as it affects WBC) has been detailed at **Appendix 1**.

4.4 A statutory consultation period has been provided within the draft settlement and which expires on 17th January 2011. The Mayor with support from the MP have provided individual responses to the Secretary of State and which are consistent with the paper at **Appendix 2**. It is unlikely the draft settlement will change but it is possible that some amendment nationally will occur due to the extreme volatility of the figures as published. It is not guaranteed that any change would benefit either Watford or other district councils.

4.5 The effects of the draft settlement have now been reflected within a revised Medium term Financial Strategy and which is covered within the next section of this report.

5.0 Medium Term Financial Strategy (MTFS) 2010/2015

5.1 The MTFS has been regularly updated and reported to Cabinet on 12th July, 1st November and 13th December (and to Budget Panel prior to these dates). At its previous meeting on December 2nd, the Budget Panel had commented upon the fact that the MTFS had assumed no increase in Council Tax throughout the four

year period 2011/2015 and had felt this was unsustainable and would put too much pressure upon necessary efficiency savings. A need to preserve current levels of service provision needed to be considered alongside a desire to contain council tax levels to the Watford community.

5.2 In reality, the draft RSG Settlement has now resulted in future increases in council tax becoming an inevitability. Attached at **Appendices 3A & 3B** is the revised MTFS which shows two different scenarios:

- Appendix 3A indicates a council tax freeze in 2011/2012, with a 2.5% year on year increase thereafter. The manifesto of the Mayor is to keep council tax increases below the level of inflation (as defined as being the Retail Prices Index/ RPI). The current level of RPI is 4.6% and is not anticipated to fall significantly during 2011/2012. It is feasible over the following three years that it will fall below the 2.5% council tax increase that has been built into the MTFS and this will need to be monitored in due course.
- Appendix 3B has continued to assume no increase in council tax over the full four year period.

5.3 In both scenarios, the MTFS has assumed no increase in council tax in 2011/2012 due to the financial incentive made available by central government if a freeze were to be instituted. This is discussed later in this report.

5.4 The major difference between the two scenarios at Appendices 3A & 3B relates to the efficiency savings required to be made. It will be recalled that the Council has been planning on the need to make £3.8m of efficiency savings throughout the four year period. The harshness of the draft RSG settlement has changed these assumptions considerably.

5.5 By reference to Appendix 3A, it should be noted that service efficiencies identified as part of the Service Prioritisation process has totalled £1.806m; £0.943m and £0.228m (totalling £2.977m) over the three year period 2011/2014. In addition it is anticipated that Shared Services should deliver a further £342k of savings to Watford as part of a Phase 2 process. The Council was on target therefore to deliver a £3.319m package of savings in order to meet the £3.8m objective and would have left a residual circa £500k to be achieved before the end of year 4. Following the RSG Settlement, the total additional savings still to be achieved comprise £49k; £19k; 436k; and £1,325k (total £1.829m) and is reflected in Appendix 3A in the line 'From/ to Reserves to fund overspend'. In reality, **further savings** will need to be identified in due course.

Appendix 3A assumes the 2.5% annual council tax increase in 2012/2013 onwards.

5.6 By reference to Appendix 3B, whilst the level of efficiency savings identified as part of the Service Prioritisation process is unchanged (£3.319m including Shared Services), the residual savings still to be identified increases over the four year period to a total of £3.088m and is almost certainly unachievable.

6.0 **Service Prioritisation Process (SPP)**

6.1 The SPP has been considered in some depth by the Budget Panel at its meeting on December 2nd and a detailed set of recommendations were referred to Cabinet

for its meeting on 13th December. Cabinet fully endorsed the recommendation of the Panel that no increase in parking permits should be introduced until a full review had been undertaken into the projected use of the car parking earmarked reserve. Apart from this adjustment all other SPP proposals were accepted for inclusion within the draft revenue estimates. (Cabinet had recommended there being no charge for using Clissold Pool but in reality this had not been included within the SPP proposals in any event).

6.2 A summary (and profiling) of SPP proposals approved by Cabinet have been attached at **Appendix 4** and have been fully reflected within the MTFS and draft revenue estimates.

7.0 Fees and Charges

7.1 Proposals for increases to fees and charges in 2011/2012 were approved by Cabinet on December 13th and broadly incorporated two principles:

- that VAT increases imposed by central government should be reflected within next year's tariffs.
- and that increases in charges should reflect the current economic climate and the limited ability for the community to absorb further increases in their cost of living.

7.2 As a consequence, the anticipated increase in income from fees and charges (other than specific targeted increases as part of the SPP process) have been negligible and a summary of the effect has been reproduced at **Appendix 5**.

7.3 Further, Cabinet has requested a review of the concessionary schemes applying across all services and this is to be considered at its meeting on January 17th. The intention being to protect as far as possible those members of the community in receipt of income support/ welfare benefit by way of differential charging for use of facilities/ services.

8.0 Draft Detailed Revenue Estimates 2011/2015

8.1 The MTFS referred to at Section 5 of this report is very much a high level planning document and the success of the process is very dependent upon detailed revenue estimates actually reconciling back to the control total assumptions reflected within the MTFS. **Appendix 6A** therefore provides a summary by cost centre of the detailed revenue estimates for 2011/2012.

8.2 The draft detailed revenue estimates at appendix 6A need to be reconciled back to the MTFS process to ensure that planning and reality are in full accord. This exercise has been reflected within **Appendix 6B**.

8.3 From this point onwards, the detailed revenue estimate figures now become the primary focus in considering levels of council tax and use of reserves for 2011/2012 and, by reference to Appendix 6A, indicates a Net Budget requirement in 2011/2012 of £14.581m. How this is to be funded is considered in later sections of this report.

8.4 The Net Budget requirement of £14.581m needing to be financed is before the

use general reserves where Cabinet has the option to reduce this level of expenditure by the use of such reserves and this is discussed in the next section of this report.

9.0 Use of Reserves

9.1 Under section 25 of the Local Government Act 2003 there is a duty on Chief Financial Officers to report on the robustness of the estimates and the adequacy of reserves when the authority is considering its budget requirement and Members are required to have regard to this advice.

9.2 The Council has accrued a reasonable level of reserves due to its prudent financial management. The full schedule of these reserves is attached at **Appendix 7**. It is, however, necessary to distinguish between those reserves that are earmarked for specific expenditures in the future and those general reserves which are available to support annual revenue budgets.

9.3 Specific earmarked reserves include where a third party has contributed to that reserve such as the Charter Place Tenants reserve; or where a reserve has a statutory limitation on its use such as the Car Parking Zones reserve; or where it is good practice to build up a reserve for a specific purpose such as the Leisure Services Corporate reserve which has been established to enable future structural maintenance to the two leisure centres to take place.

9.4 With regard to general reserves they have mostly been created to enable specific future initiatives to be financed. So, for example, the Spend to Save reserve can be accessed to pay for up front costs where a pay back saving is anticipated at a future time. This reserve was largely used to finance implementation costs relating to the shared services initiative with Three Rivers Council and which has subsequently reduced annual budgets by circa £1.2m per annum.

9.5 General reserves also need to be maintained to meet projected over spending within revenue budgets. For example, the current projection of net expenditure for 2010/2011 is forecasting a £300k overspend due in the main to the impact of the recession. If it were to occur then it is probable that part of the general reserves would be required to fund the deficit.

9.6 This of course is a crucial aspect of using reserves, in effect their use just temporarily finances a deficit. This deficit, at some point, needs to be funded from a permanent source of additional income or reduced expenditure. The use of reserves needs, therefore, to recognise they can smooth out the pace of required efficiency savings but ultimately permanent savings need to be achieved.

Factors Taken Into Account in Assessing an Appropriate Level of Reserves

9.7 It is always a difficult question regarding what are the correct level of reserves. There are some heads of expenditure which are quite volatile such as investment interest, housing/ council tax benefit, commercial rents, and future pensions liabilities. Each of these could feasibly vary significantly (and are largely outside the Council's control). It should be realised, of course, that the authority would be exceptionally unlucky to suffer adverse consequences from all major potential sources of adverse variation in the course of a financial year. An analysis of 'Key Risks' has been detailed at **Appendix 8** which should be considered before making any decisions upon the use of reserves.

- 9.8 For a district council, where changes to a few areas can have a disproportionate impact, then a higher percentage of reserves to net expenditure is desirable. Whilst a 5% cushion might be appropriate for larger all purpose authorities, it is recommended that a 15% cushion against net expenditure is more appropriate for district councils. If this recommendation were to be followed then circa £2.25m of the general available balance/reserve should be effectively frozen.
- 9.9 By reference to Appendix 7 this would indicate a residual balance of £2.241m is available to support future years revenue budgets. This however is a simplistic and short sighted approach for the following reasons:
- the Council should aim to produce a sustainable budget whereby its current expenditure is funded from current income without recourse to reserves.
 - Reserves should ideally be earmarked for new investment opportunities rather than subsidise current spending.
 - The Medium Term Financial Strategy at section 5 of this report indicates a severe reduction in Central Government Financial support from 2011 onwards and which will require further efficiencies. The need for a sufficient level of reserves to smooth such reductions in public expenditure is clearly advisable.
- 9.10 Recommendations upon the use of reserves will probably be taken by Cabinet on 17th January and the views of Budget Panel are therefore timely. In terms of meeting any shortfall in efficiency targets, it is suggested that approximately £2.241m of the general reserves at Appendix 7 is probably available to support efficiency savings over the four year period. Permanent savings will ultimately need to be realised however.

10.0 Funding of the Revenue Budget

10.1 Section 8 of the report highlighted the forecast level of revenue expenditure for 2011/2012. This section of the report indicates how such expenditure will be financed and can be summarised as follows:

- Government Grant (Revenue Support Formula Grant)
- Council Tax
- Collection Fund Surplus
- Use of Reserves
- General Fund Working Balance

10.2 Government Grant

This was discussed in detail at section 4 of the report earlier.

10.3 Council Tax Base 2011/2012

The current analysis of dwellings for the 2011/12 Council Tax Base gives a figure of 33,611 (Band D equivalent) and is based upon a 100% collection level. It is anticipated that 2011/2012 will be a difficult year for many households and an actual collection rate of 97.5% has been assumed in determining the council tax to apply next year and the Council Tax base will therefore be set at 32,771.

10.4 Collection Fund

The authority is required to review the balance on the Collection Fund annually and make an adjustment to the Council Tax for any surplus or deficit. The Collection Fund is currently projected to have a surplus of £1,082,083. As the Council Tax is also collected on behalf of HCC and Hertfordshire Police, this surplus has to be shared between all three authorities using government guidelines. Therefore, the share for each authority is as follows:

- Watford Borough Council £ 178,852
- Hertfordshire County Council £ 798,481
- Hertfordshire Police £ 104,750

Each share will reduce the sum to be raised by Council Tax next year by the individual authority.

10.5 **Use of Reserves**

This has been covered at section 9 of the report.

10.6 **General Fund Working Balance**

10.6.1 The General Fund Working Balance is very much a contingency to meet any overall outturn variation in revenue estimates for any one year. In assessing the adequacy of the level of the working balance similar considerations to the retention of reserves are made. In this instance the fact that a prudent level of reserves has been made does reduce the need for a significant level of working balance and it has generally been accepted that a balance of between 5% to 10% would be the normal range for such a contingency.

10.6.2 The level of the General Fund Working Balance as at 1st April 2011 is estimated to be £1.350 million and would represent 9% of the estimated Budget Requirement for 2011/2012. This level of balance is probably excessive in the longer term but should be retained for the two years 2011/2013 until the revised central government grant arrangements and the transfer of financing for concessionary fares have been finally resolved. Assuming no further adverse affects, then the Working Balance could be reduced to £975k (7%) of net expenditure in 2013/2014 and would mean that £375k could be utilised to smooth out efficiency savings in 2013/2014 onwards.

11.0 **Recommending the Council Tax for 2011/2012**

11.1 The level of council tax will be dependent upon the following factors:

- current level of council tax for 2010/2011
- agreed level of expenditure for 2011/2012 (Section 8 of report refers)
- use of reserves (Section 9 of report refers)
- level of Government Grant (Section 4 refers)
- the Council Tax Base at Band D equivalents (Section 10 refers)
- the Collection Fund surplus (Section 10 refers)
- use of the General Fund Working Balance (Section 10 refers)

11.2 In addition to these considerations the Mayor's strategic objective is that council tax rises should be below inflation. The relevant inflation rate, the RPI for September 2010 was 4.6%. However, Central Government has made available a

specific grant to all authorities that freeze their levels of council tax in 2011/2012. This specific grant is not 'new' money but has been top sliced from the overall amount of Revenue Support(Formula) Grant.

- 11.3 The specific grant is linked to the equivalent of what a 2.5% council tax increase would equate to and, for Watford, when the relevant council tax base and current level of council tax are taken into account, then a freeze on council tax would result in an additional grant of £204,688 and would apply for the full four year period 2011/2015. (£818,752). The only reason any authority would not take advantage of this support is if it needed a source of income in excess of a 2.5% rise in council tax. So for example, should Watford have problems in balancing its budget and needed to increase council tax by 5% in 2011/2012 then it would double the amount of income so raised (over the level of special grant) to a figure of £1.638m over a four year period. The difference being that local council tax payers would have to meet the full £1.638m whereas the additional specific grant would be financed from central government.
- 11.4 In the circumstances detailed in the previous paragraph, it would be a rather financially stretched authority that would fail to freeze council tax in 2011/2012. This additional grant has been taken off the available total of RSG Formula grant and the conditions attaching to its availability does rather throw into question the concept of 'local decision taking'. This is rather compounded in that the Secretary of State has retained the power to 'cap' excessive increases in council tax. The definition of 'excessive' is not known but any increase in council tax over 5% would almost certainly come under scrutiny.
- 11.5 Within the parameters of robust budgets and the prudent use of reserves and balances the recommended level of council tax is ultimately a political decision. To assist Cabinet/ Council in their deliberations all relevant factors are brought together in Table 1:

TABLE 1 – 2011/12 OVERALL POSITION

	£000
Net Expenditure 2011/12 (Appendix 6A)	14,581
Use of General Reserves	0
Less: RSG / Formula Grant	(6,009)
Special CT Freeze Grant	(205)
Excess Homelessness Grant	(95)
Transfer to Reserves	150
Collection Fund Surplus	(179)
Council Tax	(8,187)
Balance of Expenditure to be funded	56

- 11.6 The balance of expenditure to be funded represents the shortfall in efficiency savings required to be achieved in order to set a sustainable budget (one in balance without recourse to reserves or balances). The option to increase council tax to make good the shortfall is not possible—as this would lose all additional government grant. The remaining options are therefore to reduce next year's draft budget by adjusting any provisions such as for price inflation or by identifying

further efficiency savings. Alternatively, (and taking into account the modest nature of the shortfall) that an element of available reserves should be earmarked to cover the deficit.

12.0 Future Strategy to Meet Reductions in Government Funding

12.1 By reference to the table above and also to the MTFS at Appendix 3A, it is evident that the front loaded nature of the service prioritisation proposals has largely matched the profile of front loaded government grant reductions. The shortfall in 2011/2012 is £56k, with a further shortfall of £19k in 2012/2013. It is only in succeeding years that the continued anticipated loss in government grant will result in further efficiencies being required. The views of the Budget Panel would be welcomed regarding how a further £1.8m of efficiencies might be achieved (paragraph 5.5 refers).

12.2 Options include:

- planning for more services to be provided jointly with neighbouring authorities
- actively pursuing the competitive tendering of services (eg refuse, cleansing and potentially property management and maintenance).
- accepting the need to use an element of the Council's available reserves on a phased basis to spread the period over which efficiencies need to be made.
- increasing council tax over and above the assumed 2.5% uplift built into the MTFS

12.3 Budget Panels views regarding its preferences would be welcome.

13.0 Capital Programme 2010/15

13.1 The Capital Programme was considered and approved by Cabinet at its meeting on 13th December and is largely a continuation of the existing programme with the addition of additional provision where rolling programmes are involved. The programme and its financing is attached at **Appendix 9** for Budget Panel information/ scrutiny.

14.0 CONCLUSIONS

14.1 The Budget for 2011/2012 (and indeed for 2012/2013) appears to be very much in balance at the present time. This has only been achieved due to the thorough financial planning process and the methodical way in which service prioritisation proposals have been considered and agreed. It is essential that all those proposals are delivered within profiled timescales and implementation plans need to be closely monitored.

14.2 For 2012/2013 and future years it has now been assumed that an average 2.5% year on year increase in council tax will be necessary in order to part compensate for the severe reductions in government grant. This clearly will need to be reviewed on a year by year basis at the appropriate time.

14.3 The biggest challenge would appear to be to produce sustainable budgets in the two year period 2013/2015. No firm information is available about further grant

losses in those years but assumptions have been made based upon the Comprehensive Spending Review produced by Central Government in October 2010. The key to continuing to meet further pressures is to have a longer term strategy regarding how services can be protected as far as possible whilst reducing cost bases.

15.0 FINANCIAL IMPLICATIONS

These are adequately covered within the report.

16.0 LEGAL IMPLICATIONS

These are adequately covered within the report.

17.0 POTENTIAL RISKS

These are adequately covered within the report.

Appendices

Appendix 1	Summary of Draft Revenue Support Grant Settlement (as it affects WBC)
Appendix 2 / 2A	Draft RSG Settlement Consultation – WBC Representations
Appendix 3A	Revised Medium Term Financial Strategy
Appendix 3B	Revised Medium Term Financial Strategy (no increases in Council Tax)
Appendix 4	Service Prioritisation Proposals
Appendix 5	Summary Schedule of Fees & Charges
Appendix 6A	Draft Detailed Revenue Estimates 2011/12
Appendix 6B	Reconciliation of Draft Detailed Revenue Estimates to MTFS
Appendix 7	Schedule of Reserves
Appendix 8	Key Risks
Appendix 9	Capital Programme 2010 – 2015

Background Papers

Budget Working Papers

File Reference

None