

Report to: Budget Panel
Date of meeting: 10th September 2013.
Report of: Shared Director of Finance
Title: Revised Medium Term Financial Strategy 2013 / 2018

1.0 SUMMARY

1.1 This report provides an overview of financial issues affecting the Council over the period up till March 2018 and enables a strategy to be developed to achieve a sustainable budget and set a Council Tax for 2014/15.

2.0 RECOMMENDATIONS

2.1 To consider the attached report.

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3.0 INTRODUCTION

3.1 The Medium Term Financial Strategy (MTFS) provides an overview of the main components of Watford's revenue expenditure and available finance. For the document to be meaningful for financial planning it is necessary to forecast likely scenarios over a medium term perspective (four years 2018). The current policy of the Council is to produce a sustainable budget by the end of that four year period.

Cabinet at its meeting on 8th July considered an update on the MTFS and which included a number of actions that needed to take place between July and September.

This paper indicates the progress that has been made and provides a position statement that must be further reviewed as budget planning evolves.

The revised MTFS is attached at **Appendix 1**.

3.2 This is an up-dated version of the MTFS following recent government announcements. This is not the finished product and will be refined during the Autumn as more information becomes available.

The MTFS reflects the current expenditure base and then applies any year on year variances. So, for example, the very first item at Appendix 1 (ICT Capita Outsource) indicates a £136k reduction to our base estimates in 2014/2015 (which is then reflected within the opening base estimate for 2015/2016). In 2015/2016 there is a further £97k saving, so that we commence the 2016/2017 with a cumulative base reduction of £233k.

With regard to the Funding Section of the MTFS, each year is treated separately so that it is straightforward to see the profile of our funding streams over a four year period.

3.3 Expenditure Projections

The MTFS included at Appendix 1 includes a number of variations to expenditure projections. These are detailed below:

ICT: The current MTFS assumes that there will be a savings in this service due to changes in service provision. However, these savings will not materialise in 2013/2014 because it was identified during the tendering process that no improvement to the ICT service would be possible without considerable up front investment. WBC's contribution to this improvement will be £317k drawn from the Invest to Save Reserve as a one off funding source. This can be seen in the Month 4 Finance digest which is elsewhere on this agenda.

Council Road Map Efficiencies: a target £2m saving had been set from various initiatives (albeit a £350k contingency for non achievement had

been built into the MTFS). A number of initiatives have now been achieved and these will be analysed in the context of the £2m target. There is however undoubtedly a case to continue to identify further savings (and indeed to review support costs in the light of all outsource activity). A target £400k to be achieved in 2015/2016 has been included within the MTFS at this time.

Waste: this reflects the reduced cost of the service provision compared to the existing budget due to a change in the service provision arrangements.
DCLG Grant: this is due to cease in 2015/16.

Commercial Rents have been estimated to increase by £330k in 2013/2014, but reducing by £100k in 2014/2015 primarily due to Health Campus development which will impact on Cardiff Road businesses.

Reduced investment interest has been included due to the continuing low interest rates and profile of capital programme.

Building Control: It is anticipated that a saving of £150K can be achieved through a change in service provision of this service.

Indoor/ Outdoor Market: it is estimated that there will be a saving of £230K from 2013/14 following a change in provision of these services.

The CCTV Relocation is anticipated to generate a saving of £120k in 2014/15.

Elections: reflects the cyclical nature of elections.

Watford Business Park – the anticipated savings of the pay and display scheme.

Housing Related – savings anticipated to be achieved through retendering exercises and other savings.

Shared Services Operating Costs—this reflects a paper that went to Shared Services Joint Committee in November 2012 and includes £250k for additional resource (one year only) for Revenue and Benefits staffing/ agency.

Revenues and Benefits Client Account: Additional costs related to the provision of this service.

Pay Inflation – A 1% year on year increase. Should a pay award exceed 1% then the current vacancy levels may need to be reviewed.

Employers Superannuation - there will be an actuarial review as at March 2013 (results in December 2013) and the MTFS has assumed an effective 2% increase in employer rates in 2014/2015.

Contracts/ Fuel - this will need to be reviewed in more detail through the Autumn.

Fees and Charges - a nominal £20k per annum additional income has been built into the MTFS in 2014 onwards - but this needs to be reviewed throughout the Autumn.

West Hertfordshire Crematorium: It is anticipated that the service will be able to generate a £50k per annum surplus to each constituent authority - commencing in 2014/2015.

Ongoing Procurement Saving: a feature of the 2012/2013 Outturn was a significant procurement saving - particularly on gas and electricity. This should result in a permanent base adjustment of £200k.

Borrowing Costs, Minimum Revenue Provision: this reflects the Councils anticipated costs of borrowing to fund capital expenditure.

Health Campus: this reflects the anticipated returns from this scheme.

3.4 **Central Government General Support.**

For 2013/2014 the MTFS included the receipt of £5,724k by way of Formula Grant/ NNDR and Council Tax Reduction Grant (£4,765k; and £958k respectively).

The Chancellor of the Exchequer announced on 26th June 2013 public expenditure targets for 2015/2016 (one year only, to be reviewed for future years after a General Election). For local authorities the headline figure was a further 10% reduction in government support and which can only be assumed will include a reduction in the council tax benefit reduction element which has now been subsumed within the general external support.

Further information has emerged and there are a number of exemplifications available which model projected settlement figures based on the technical consultations for the 2015/16 local government financial settlement. For Watford the reduction in funding is estimated to be 14.6% if the full impact of the changes materialises. This compares to an 8% reduction included in the previously reported MTFS update. The MTFS has therefore been revised to reflect these increased funding reductions. This 2014/15 funding figure is therefore estimated to be £4915K, which is £48K less than originally anticipated. There have been similar reductions in 2015/16 funding which are estimated to be approximately £400K worse than previously reported.

Following on from this the funding reduction for 2016 onwards have also been increased and are based on a 20% reduction in Revenue Support Grant. As the Business Rates income has been fixed, any further reduction in government support must come solely from the Revenue

Support Grant. However, this will be kept under review.

3.5 **Business Rates Retention**

One of the major changes to local government funding has been the incentive for local authorities to grow their business rates base. Formerly all business rates income was collected on behalf of central government and then redistributed back to authorities on the basis of need. This however provided no incentive for local authorities to seek to maximise business rates income or indeed improve their collection rates.

The Business Rates Retention system has now been set and cannot be changed. There are a number of risks which have been transferred to local authorities as a result of the new system. The financial impact of some of these risks may be large and could have a significant impact on the MTFS. The Government have set a maximum exposure level for local authorities, 7.5% of their original 'baseline' position. However, whether these risks will materialise is still to be seen.

Watford is currently involved in a number of large scale redevelopment projects, which may in the short term, have an adverse impact on the level of business rates payable. These have been estimated and are built into the MTFS.

As a result there is a short term reduction in business rates included in the MTFS. This situation will be kept under review and as we get more clarity over the actual position the MTFS will be updated.

3.6 **New Homes Bonus Grant**

The government has set a priority to build more homes and to encourage authorities to make more land available / and to facilitate development. As a consequence, a significant amount of funding has been made available for authorities that produce a net increase in available homes in any one year. The funding to be distributed and called 'New Homes Bonus Grant' and the size of any individual distribution to be related to past achievement in the previous year.

The available funding is not 'new' money but has been generated by top slicing it from general Revenue Support Grant. This redistribution has not been appreciated by the less prosperous parts of the country (typically the north east) where there is little residential development actually being constructed. The south east has been the main beneficiaries with Watford having received significant amounts of NHB.

It is necessary to review our current model relating to the future receipt of NHB and this will involve firstly an internal review to determine the net number of additional units (this is effectively those properties coming on stream less those properties lying empty). There is also a premium if the

units are deemed 'affordable' so that needs to be evaluated at the same time.

The current MTFS has been based upon historic data and needs to be revisited (for example, the net number of housing completions in 2012/2013 was 541 homes whereas the NHB model has assumed 408 net completions. Any review needs to involve the Planning Policy Team, the Housing Division, a representative from Revenues, and financial back up. Ideally the results of this review should feed through to the revised MTFS in September.

The Chancellor's statement on 26th June 2013 was silent regarding the New Homes Bonus but made much play of the fact that £2bn is to be made available in 2015/2016 onwards for the creation of a Single Local Growth Fund with funding for transport, skills, and housing and to be allocated through the Local Enterprise Partnerships. Subsequent clarification has been received that £400m of this £2bn is to be top sliced from New Homes Bonus (estimated at 30% of total NHB). This is extremely disturbing news for Watford as the £2bn may well be redistributed from the South East and this again will need to be reflected within the revised MTFS.

A consultation paper has been issued which identifies how the 'top slice' may operate. As specific details have not been announced no amendment to the NHB figures have been made at this stage. We will update the figures once it is clearer what the size of the top slice will be. Therefore the NHB figure is likely to be overstated.

3.7 Council Tax Freeze grant

The current situation is that the MTFS in 2014/2015 includes £204k of freeze grant that relates to the initial freeze guarantee made in 2011 that if authorities froze council tax in 2011/2012 they would receive freeze grant equivalent to a 2.5% increase in council tax for the four years 2011/2015.

In the 2013/14 settlement and confirmed by the 2015/16 settlement technical consultation the original Council Tax freeze grant has been included in the 'Start Up Funding Assessment' and has therefore been rolled up into the Revenue Support Grant and the Business Rates Baseline and will continue past 2014/15. We have therefore extended the period in which this money will be received through to the end of the MTFS period.

The 2015/16 settlement consultation also indicates that for authorities which chose to freeze their council Tax in 2013/14 there will be an extension of the funding. We have also extended the timeframe over which we estimate this grant will be received through to the end of the MTFS period. This grant is equivalent to a 1% council tax increase.

The Chancellor of the Exchequer, in a statement to the House of Commons on 26th June, announced that grant would be available for councils freezing council tax in 2014/2015 and 2015/2016 and will almost certainly be geared

to a 1% tax increase (£80k using new tax base). This needs clarification however as it is uncertain whether there will be a further grant in 2014/2015 in addition to what has been assumed and also the cumulative position in 2015/2016. We have not included anything in the MTFS in relation to this grant for this as a decision on Council Tax levels still needs to be made. However, we have assumed a nil increase in Council Tax for planning purposes.

The Chancellor also announced that council tax capping will continue to apply and that a referendum will be required should the council tax increase by more than 2% (assumed to affect 2014/2015 as well as 2105/2016). It is probable that some authorities will actually test the 'will of the people' in 2014/2015.

3.8 Council Tax Base, Collection Fund and Collection Levels

Within the current MTFS, the council tax base for 2013/2014 was estimated to be 29,418 Band D equivalents with annual increase of 350/ 350/ 250 in the three years 2014/2017. The latest schedule of council tax indicates that the base for 2013/2014 will actually be 30,007 and shows a 589 (Band D equivalent) increase to the base and equates to an additional £147k income for Watford services (and which will be ongoing throughout the MTFS period).

Whilst this is a reliable starting point, it is important that future projections of growth in the council tax base mirror assumptions within the Planning Policy Division regarding future residential development projects (including the Health Campus).

The Collection Fund is a statutory account which charts the amount of council tax anticipated to be collected against the amounts actually collected. The MTFS has made no assumptions for either surpluses or deficits on this Fund throughout the four year period. This needs to be reviewed (the outturn for 2012/2013 indicates a £189k surplus was recorded (£31k to Watford, the rest to the preceptors).

Finally the MTFS needs to review collection levels of council tax to seek to establish are they still realistic (97% collection rates has been assumed throughout the four year period).

3.9 Salaries and Associated Costs

The total salary and agency bill in 2012/2013 was circa £14.5m but, paradoxically, is often one of the easiest to control. If the budgets were forecast to overspend then a recruitment freeze can be introduced. The current MTFS has assumed a 1% vacancy level across most services .

The MTFS also has to make provision for future pay awards and had allowed for an effective 2% award in 2013/2014 and 1% a year thereafter.

It is likely that local government trade unions will accept a 1% award from 1st April 2013 (with an additional 1.4% for the lowest paid). Watford has no staff that fall within the definition of 'low paid' so we are likely to have a 1% cushion within our revenue budget.

The Chancellor of the Exchequer announced on June 26th that the public sector would be limited to a 1% pay award in 2015/2016 (which although not binding on local government, does generally set a benchmark). The Chancellor has also announced that there will be no automatic progression (increments) permitted in future for the civil service, schools, hospitals, prisons and the police. Again he has no direct control over local government but the Secretary of State at the DCLG may adjust government funding to achieve the same effect. In reality, for Watford, most staff are on the top point of their grades so the financial effect would be limited either way.

Of far greater concern however is the future effect upon the salaries bill of potential changes to employers contributions to national insurance where government pronouncements need to be carefully analysed as no additional cost has been reflected within the MTFS.

Similarly, there is to be an actuarial review of all local authorities pension schemes as at 31st March 2013 (results known in December 2013) and it is widely anticipated that current deficits will have increased due to the combination of people living longer and poor investment returns due to the 'low interest rate' environment. Watford has always followed the HCC actuary's advice which aims to cover any deficit over a 20 year perspective. The current MTFS had anticipated an increase in employer contribution rates by 1% in April 2014 and again by a further 1% in April 2016. The April 2016 increase may have to be brought forward to April 2014 and this needs further evaluation.

3.10 **Goods and Services**

The MTFS has generally expected Heads of Service to live within cash limited budgets (if inflation goes up, volumes must go down). In reality improved procurement and consequent lower unit costs has meant this has not been a pressure area.

This cash freeze has not been applied to energy/ fuel costs where a 10% a year increase has been built in. Similarly business rates on our own properties has been allowed (2.6% for 2013/2014) and welfare payments such as housing benefit has also taken into account annual uplifts; and finally where there are outsourced contracts with an inflation factor then this has been applied.

3.11 **Cost of Welfare Benefits**

Unquestionably the most volatile, uncertain and high risk area of the Council's revenue budgets. Recent changes include a reduction in subsidy

for council tax benefits, implementation of a benefit cap, and withdrawal of an element of benefit where there is an under occupation of bedrooms. For the future, there will be the phased implementation of universal credit with the transfer of responsibility for administration from local authorities to the HMRC. This could well affect levels of staffing but the current timescales may well slip. An evaluation does need to take place as the potential effects of universal credit have not been factored into the MTFS. However, the anticipated national roll out of Universal Credit in October 2013 has been delayed and the full impact of this is not yet known, as such no changes to the income or expenditure for this service have been included in the MTFS.

This position will be updated once a clearer picture is available.

3.12 **Reserves**

The estimates included at Appendix 1 indicate that there will be approximately £3.0M drawn down from general fund Reserves over the period 2013-2018.

The anticipated position on Reserves as at the end of 2013/14 is attached at Appendix 2, this is the estimated position before any drawing down to meet any budget shortfalls. The Appendix also shows future 'commitments' which include:

- £380k being the winding up of the Charter Place Tenants Reserve
- £317k to fund up front Capita ICT work
- £1,542k being first tranche of £3m towards Health Campus LABV
- £1,500k to fund the New Market
- £313k to fund vehicle and plant
- £285k from Veolia to also fund vehicle and plant.

Should we need to draw circa £3m from Reserves in 2013/2018 then our reserves will be reduced to £7.5m (plus a General Fund Balance of £1.350m). Some of these reserves are specifically earmarked (CPZ).

A full review of reserves should be undertaken in the next few months to ensure that they are still required for purpose for which they were created.

It is important to emphasise that the use of reserves can only be considered as a short term expedient and that, at some point, the need to balance expenditure and available ongoing funding will be of critical importance to the financial resilience and health of any local authority.

3.13 **Conclusion**

The aim of the MTFS is to provide a reliable forecast over a four year planning timescale to enable a sustainable financial environment to be in

place where ongoing expenditure and income are in tandem. The MTFS can only be as good as the assumptions and realism reflected within it. Should an over optimistic view be taken then, in the fullness of time, shortfalls in funding will appear and reserves or knee jerk service reductions will be necessary. Equally however an overly pessimistic view will probably result in a greater degree of service reductions being imposed. It is a balancing act and that is why the MTFS should be reviewed on a regular basis.

The MTFS will be kept under review during the autumn and will be further refined as we move towards setting the Council Tax so as to provide as accurate a forecast as possible in terms of further income and expenditure projections.

4.0 FINANCIAL IMPLICATIONS

4.1 Included in the report.

5.0 LEGAL IMPLICATIONS

5.1 There are no legal implications included in the report.

6.0 POTENTIAL RISKS

Potential Risk	Likelihood	Impact	Overall Score
That the Medium Term Financial Strategy will be based upon unreliable data	2	4	8

7.0 EQUALITIES

7.1 Watford Borough Council is committed to equality and diversity as an employer, service provider and as a strategic partner. In order to fulfil this commitment and its duties under the Equality Act 2010 it is important to demonstrate how policies, practices and decisions impact on people with different protected characteristics. It is also important to demonstrate that the Council is not discriminating unlawfully when carrying out any of its functions.

The reporting of issues that need to be reflected within a review of the Medium Term Financial Strategy does not equate to actually making any firm proposals and will not therefore have equality implications.

Appendices

- Appendix 1 - Revised Medium Term Financial Plan 2013-2018
- Appendix 2 - Reserves