

Executive

Medium Term Financial Strategy (MTFS) Update

24 May 2010

Report of the Head of Finance

PURPOSE OF REPORT

The Medium Term Strategy (MTFS) is the Council's key financial planning document. It is driven by our Corporate Plan and the four strategic priorities which lie at the heart of it. The 2010/11 local government finance settlement represented the final year of the "fixed" three year funding regime announced in 2008/09. Due to the current economic climate and national deficit it is clear that local authorities will continue to need to plan on the basis of a very restricted financial envelope from 2011/12 onwards. This report considers 3 scenarios for funding and calculates the potential shortfalls which will need to be addressed to deliver a balanced budget.

This report is public

Recommendations

The Executive is recommended:

- (1) To note contents of report and MTFS scenarios detailed in Appendix 1.
- (2) To note the process and approximate timings of the Formula Grant Settlement and Concessionary Fares Transfer Impact
- (3) To agree that we should lobby Department of Communities and Local Government (DCLG) with our counterparties in Oxfordshire and approach Northamptonshire for a joint approach on the financial implications of the concessionary fares transfer.
- (4) To agree that each MTFS scenario modelled will have a specific action plan developed to address the projected shortfall.
- (5) To advise of any other scenarios they would like modelled and / or matters they would like taken into consideration in developing the action plans.
- (6) To agree Timetable and process for the development of the next MTFS forecast and action plans.

Executive Summary

Introduction

- 1.1 The MTFS is a key part of the Council's Policy, Service Planning and Performance Management framework which aims to ensure that all revenue and capital resources are directed towards the Council's strategic priorities.

The Strategy describes the financial direction of the Council for planning purposes and outlines the financial pressures over a 4 year period.

- 1.2 The MTFS establishes how available resources will be allocated to services in line with Council priorities following extensive consultation with Councillors, residents and other stakeholders.

Proposals

- 1.3 We continually update our medium financial strategy and model scenarios to test our planning rigorously and the latest forecast can be seen along with assumptions in Annex 3 of the 2010/11 budget book. The draft forecast – best case at present (ref – column D Line 52) shows a forecasted shortfall of £1.2m from 2010/11 to 2011/12. This annex also shows an analysis of reserves, capital receipts, cashflow and the impact of the capital programme. Our capital receipts are forecast to reduce from £42m to £21m by March 2015 based on the current capital programme.
- 1.4 This report considers these assumptions in light of the current economic climate, change of government and expected reduction in government grant funding. This report consider 3 scenarios (best case, worst case and realistic case) in order to allow the Council to produce action plans to meet the shortfalls in each scenario. The timing of the government settlement is not due until November 2010 so a number of assumptions have been made to ensure we begin our deliberations and planning early.
- 1.5 The detailed assumptions that have been modelled are shown in Appendix 1 but at present our best case scenario assumes a freeze for the next 3 years and our worse case assumes a 6.5% cut in each of the 3 years – effective 19.5% with no inflationary increases.
- 1.6 The other consideration that we need to understand further is the impact of the transfer of concessionary travel to the County as this will be considered in the next formula grant settlement. It is imperative that we have an input into these calculations ahead of formal consultation as the revenue support grant reduction for concessionary fares should be no more than Cherwell District Council received to run the service in the first place.
- 1.7 In order to be prepared for the impact of the forthcoming funding decisions from the new Government and potential shortfalls that will arise the Council needs to develop an action plan for each scenario. This action plan needs to be robust and have a clear indication of how the Council will deliver a balanced budget and which services will be prioritised.

The action plan should consider:

- 1) Sources of funding
- 2) Review of service priorities
- 3) Statutory / Discretionary Service Review
- 4) VFM and Improvement Programme
- 5) Review of capital receipts and capital priorities
- 6) Collaboration and Partnership Opportunities

- 1.8 In order to produce these plans extensive consultation is required with Members, Residents of the District and our partners. This consultation will begin with a workshop with the Executive in July 2010.

Conclusion

- 1.9 Whilst not underestimating the major challenges ahead facing the Council, it is better placed than many Councils to respond to the challenges posed by the wider economic situation, as during the previous period of economic growth not only did the Council continue to realise efficiency savings but also focused on delivering value for money services whilst reducing support costs.
- 1.10 Whatever the level of cuts determined by the Government, local decision makers will face extreme pressure to implement necessary changes and deliver required savings on challenging timetables. In this context it is critically important that we anticipate these developments and prepare for them.
- 1.11 The Council will make formal responses to the concessionary fares consultation and the Settlement Working Group consultation during the summer and produce an updated MTFS forecast and robust action plan to address the shortfall and present these to the Executive in October 2010 ahead of the 2011/12 budget process.

Background Information

Medium Term Financial Strategy – Background

- 2.1 Our current Medium Term Financial Strategy was approved by the Executive in April 2009. This strategy committed the Council to eliminating its revenue dependency on investment income within the remaining 4-year lifetime of the strategy. This required some limited and reducing support from reserves during the period to ensure effective implementation while protecting service levels during any transition period. A number of potential actions were identified to secure the required reduction in net expenditure over the duration of the strategy – circa £2.6m.
- 2.2 The MTFS financial forecast is reviewed and refreshed on an annual basis and was last agreed by the Executive as part of setting the 2010/11 budget in February 2010. Cherwell District Council is committed to maximising the use of scarce resources and directing resources towards its priorities whilst keeping Council Tax at an affordable level. The main driver for the MTFS is the desire to provide high quality services that are in the line with Council priorities and resident needs at the least possible cost to council tax payers.
- 2.3 The MTFS flows from the Sustainable Community Strategy and the Corporate Plan and shows what the Council will do to ensure a stable and sustainable financial position that will allow the Council to achieve its vision and strategic objectives over the next three years, delivering on the key objectives of value for money and efficiency, continuing to deliver the Council's commitments to below inflation council tax increases and high quality services for the residents of our District. Maintaining the Council's financial strength will ensure the delivery of services is maintained during a period of economic uncertainty.
- 2.4 The MTFS assumptions are being reviewed to take into account the effects of the national economic situation. RPI and CPI measures of inflation have been volatile over the past 12 months and the Bank of England has kept the bank base rate at 0.5% for the last 13 months. Whilst CPI is expected to reach its target of 2% over the next 2 years it will do so as interest rates increase.

- 2.5 The level of Government debt is forecast to grow to nearly 80% of GDP. It is widely acknowledged that public expenditure will need to be reduced significantly, certainly for the period of this MTF5 and probably longer i.e. at least the next two CSR spending rounds. The Government announced in the Pre-Budget Report (PBR) that some services would be protected but local government has not been mentioned in this context and can expect to bear the full impact of any reductions.
- 2.6 This is likely to translate into a reduction in Formula Grant and an even greater reduction in specific grants related to specific initiatives and in capital funding, which will impact upon the resources available for the Council to deliver services. The PBR stated that capital spending was 3.3% of GDP in 2009/10 but will move to 1.25% of GDP by 2013/4 – a reduction of over 60%. Other major income streams are also under pressure whilst the demand from the public for a diverse range of good quality services will continue.

Formula Grant Settlement Process

- 2.7 There have been a number of discussions raised at Executive during the 2010/11 budget process regarding how difficult central Government funding for local government might be going forward and how we might build this into our medium term financial strategy. In relation to future settlements, known as the Formula Grant Settlement, there are two critical elements - what the size of the settlement will be for local government and how it will be distributed. There are 4 stages to the process and these stages are outlined below:

1) Comprehensive Spending Review.

This activity will be one of the first tasks of the new coalition government and will be led by Eric Pickles MP who has been appointed secretary of state for communities and local government. The Coalition Government has announced that there will be an emergency budget is expected within 50 days. There are no details in relation to this yet but they have indicated that they will be reviewing the long term affordability of public sector pensions. Therefore the outcome of a spending review is expected in the autumn.

In the Spending Review, the Government decides how much it can afford to spend over the period 2011/12 to 2013/14 and reviews its expenditure priorities. It sets the framework for Government grant support to local government and specifies the total level of grant that will be paid for the following three years. This will only provide a high level overview of grant support and it is not possible to estimate at this stage what levels of Formula Grant the Council will receive over the next three years.

2) Settlement Working Group (SWG)

The next stage will be the outcome of the Settlement Working Group who are set up to discuss issues relating to formula grant distribution, in particular potential changes to the 2011-12 Local Government Finance Settlement onwards. They are also tasked with arranging the transfer of concessionary travel to the County and associated impact on support grant.

This is a Working Group of:

- Departmental officials,
- officials from other Government departments,
- officers from the LGA,

- officers from London Councils,
 - representatives of the Local Authority Association Special Interest groups, and
 - representatives of the Treasurers Societies
- 2.8 Their work to date can be seen in the minutes of their meetings available on the Department of Communities and Local Government (DCLG) website. The outcome of this work will be the **Settlement Working Group Consultation Report**, which will probably come out in September 2010.
- 2.9 This technical report will set out a series of options for changes to the formulae, which are used to allocate out grant to local authorities. It will also show how each option will impact on councils. This is a key report because after the consultation exercise has been completed, the report is duly amended and then passed to Ministers to take final decisions on the options for change. We have the opportunity to provide a formal Council response to the consultation and this response will come to the Executive in September or October 2010.
- 2.10 Once we receive this report we will be able to model some further MTFS scenarios but these will be indicative at best for a number of reasons. Firstly, for each change under consideration there will be a number of options, which will have a varying impact on the Council's grant. Secondly, the Consultation Report will not set out how much grant will be allocated to each specific service such as social care and highways, which can have a significant effect on how much total grant is eventually allocated to the Council. Finally, it will not set out how the system of grant floors will operate, which will be key in determining our final grant entitlement. Unless there are radical adverse changes to the formula used to allocate out the grant, we will not be on a floor in 2011/14 but we will have to make a contribution to the floor scheme, which will in turn reduce the grant that we receive.

Provisional Finance Settlement

- 2.11 The next stage in the process is the publication of the **Provisional Finance Settlement** in late November/early December 2010. It will be these figures that we use for the preparation of the 2011/12 budget. This will specify the Council's proposed grant for the following three years. After the publication, there is another period of consultation, when local authorities can put their views on the proposals to Government, and point out any errors that may have been made. Once all the points from local authorities have been considered and any amendments have been incorporated, the final Local Government Finance Settlement is approved by the House of Commons in late January or early February. In previous years there have been only very minor changes to the Provisional Finance Settlement grants as the consultation at this stage, focuses on data errors rather than on changes in the formula; and so we will be able to plan with some confidence, on the basis of the three-year grant entitlements released in November/December. We will then know with certainty when the Final Finance Settlement is published, what grant we will actually receive in 2011/12.

Final Local Government Provisional Finance Settlement

- 2.12 The Final Local Government Finance Settlement published in January/early February 2011 will only contain final grant figures for 2011/12. It is not possible for the Government to announce final 2012/13 and 2013/14 formula grant allocations at this time without a change in the law. As a result, unless

there is a change in the legislation, the Government will announce the final 2012/13 and 2013/14 formula grant allocations in Jan/Feb 2012 and Jan/Feb 2013, respectively. However, using the example of the last two Settlements, the 2012/13 and 2013/14 grants announced in the Provisional Settlement in November/December 2010 will probably not change.

Concessionary Fares Funding Implications

- 2.13 The DCLG website reveals that there are 6 options that have been considered so far by the Settlement Working Group (SWG) for transferring the service to Upper Tier Authorities and each has a financial implication of formula grant reductions for Cherwell District Council. The current options have an impact of between £1.3m and £0.8m; this is on top of any expected reductions in government grant due to the spending review.
- 2.14 The DCLG have always said and continue to say that the revenue support grant is complicated and it is not possible to say how much is for each individual service but using the information available on their website and using the approach Northamptonshire authorities have taken it is possible to make a comprehensive calculation showing the amount of funding Cherwell received in 2006/07 for concessionary fares. This calculation equates to £0.9m which at today's prices (inflated using the formulae grant annual uplifts) would equate to £1.1m of funding reductions and a further £0.2m of loss of special grant. Using these figures and offsetting against expenditure would result in a budget pressure of £0.3m.
- 2.15 The pre-budget report in December 2009 said further detailed calculations will continue with the SWG and consultation will commence in July 10. Cherwell District Council are currently exploring how we can work with the Local Government Association, Society of District Treasurer's and our contacts within concessionary fares to feed into this group. We hope to agree with all neighbouring districts and Northamptonshire that we should make a group representation to DCLG prior together with to any formal consultation.

MTFS Scenarios

- 2.16 The funding pressures that the Council faces in the medium term are not unique; they are facing all Councils across the country, posing the challenge of delivering priority services within tightening resources available.
- 2.17 Eliminating our revenue dependency on investment income reduces the impact of low returns and enables the Council to utilise this income in a number of different ways, including:
- Growing the capital base to allow for future investment
 - Funding capital financing arrangements for major scheme
 - Funding short-term one-off revenue based activities in the future
- 2.18 Cherwell District Council faces a period of funding restraint and in the MTFS model the Council, like other Councils, is forecasting on this basis. The MTFS model provides the latest indication of financial pressures for the period 2011/12 to 2014/15.
- 2.19 Whilst we await the outcome of the spending review, impact of the change of government and an indication of level of government grant we can expect a variety of planning scenarios have been modeled and for the purposes of this report 3 indicative scenarios are set out:

Scenario 1 - Best Case

2.20 Key assumptions are as follows:

- Formula grant is frozen at 2010-11 levels – no inflation so real term cut
- Concessionary Fare Transfer poses a budget strain of £320k
- Pension fund triennial valuation poses 3% increase phased over 3 years
- Grants such as Area Based Grant and Local Authority Business Growth Incentive (LABGI) continue to be received and fund short term projects only.
- Assumption that Housing Planning Delivery Grant (HPDG) is removed.
- Council Tax increases at 0.5% less than RPI
- Continue to reduce reliance on investment income

Scenario 1 - BEST	2011-12	2012-13	2013-14	2014-15
	£M	£M	£M	£M
Net Expenditure	19.4	19.1	18.8	18.7
Gov't Grant	-10.9	-10.9	-10.9	-10.9
Council Tax	-6.4	-6.6	-6.8	-7
Investment Income	-0.4	0	0	0
Collection fund	-0.1	0	0	0
Use of Reserves	-0.5	-0.3	0	0
Savings requirement	1.1	1.3	1.1	0.8
RPI	3.00%	3.50%	3.00%	3.00%
Payroll Inflation	1.80%	1.90%	3.00%	3.00%
Interest Rate	1.00%	3.00%	4.50%	4.50%
Council Tax Increase	2.50%	3.00%	2.50%	2.50%

Total shortfall to identify over 4 yr period is **£4.3m** assuming efficiencies are achieved at 4% annually this would leave a medium term revenue plan deficit of **£1.1m**. This equates to further base budget annual reduction requirement of approx **£300k**. This equates to **1.5%** of base budget.

Scenario 2 - Worst Case

2.21 Key assumptions are as follows:

- Formula grant is cut in accordance with CIPFA / SOLACE model of 6.5% reduction for each of the 3 years (19.5% reduction)
- Concessionary Fare Transfer - budget strain of £1.3m – worst SWG option
- Additional grants are all reduced to zero
- Pension fund triennial valuation poses 5% increase phased over 3 years
- Interest income reliance, RPI, Payroll Inflation, Interest Rates and Council Tax assumptions as per scenario 1

Scenario 2 - WORST	2011-12	2012-13	2013-14	2014-15
	£M	£M	£M	£M
Net Expenditure	20.5	20.5	20.3	20.1
Gov't Grant	-10.2	-9.5	-8.9	-8.9
Council Tax	-6.4	-6.6	-6.8	-7
Investment Income	-0.4	0	0	0
Collection fund	-0.1	0	0	0

Use of Reserves	-0.5	-0.3	0	0
Savings requirement	2.9	4.1	4.6	4.2

Total shortfall to identify over 4 yr period is **£15.8m** assuming efficiencies are achieved at 4% annually this would leave a medium term revenue plan deficit of **£12.6m**. This equates to further base budget annual reduction requirement of approx **£3.1m**. This equates to **15%** of base budget.

Scenario 3 - Realistic Case

2.22 Key assumptions are as follows:

- Formula grant is cut by 5% for each of the 3 years (15% reduction)
- Concessionary Fare Transfer poses a budget strain of £0.8m – mid range option per SWG
- All additional grants such as Planning Delivery Grant, Area Based Grant and The Local Authority Business Growth Incentive (LABGI) grant are reduced to zero
- Pension fund triennial valuation poses 3.3% increase phased over 3 years
- Interest income reliance, RPI, Payroll Inflation, Interest Rates and Council Tax assumptions as per scenario 1

Scenario 3 - REALISTIC	2011-12	2012-13	2013-14	2014-15
	£M	£M	£M	£M
Net Expenditure	19.9	19.6	19.4	19.3
Gov't Grant	-10.4	-9.8	-9.3	-9.3
Council Tax	-6.4	-6.6	-6.8	-7
Investment Income	-0.4	0	0	0
Collection fund	-0.1	0	0	0
Use of Reserves	-0.5	-0.3	0	0
Savings requirement	2.1	2.9	3.3	3.0

Total shortfall to identify over 4 yr period is **£11.3m** assuming efficiencies are achieved at 4% annually this would leave a medium term revenue plan deficit of **£8.3m**. This equates to further base budget annual reduction requirement of approx **£2.1m**. This equates to **10.5%** of base budget.

2.23 All of the scenarios above include an annual uplift on fees and charges only and do not include any additional income in relation to Bicester Town Centre development or additional income from Council properties. This will be included in the next development of the financial forecasts and outlined in the action plans.

Sensitivity Analysis

2.23 A small change in key underlying assumptions can produce a significant change in the budget. The key sensitivities are outlined below:

Sensitivity	Change	Annual impact
Pay award	1%	£120K

Inflation	1%	£120K
Government grant	1%	£110K
Pension Rates	1%	£125K

2.24 The detailed scenarios financial forecasts have been produced using the MTFS model. This model also shows an analysis of reserves, capital receipts, cashflow and the impact of the capital programme. Our capital receipts are forecast to reduce from £42m to £21m by March 2015 based on the current capital programme and plans to replenish these are required.

Action Plans

2.25 In order to be prepared for the impact of the forthcoming funding decisions from the new Government and potential shortfalls that will arise as a result of the scenarios modelled the Council needs to develop an action plan for each scenario. This action plan needs to be robust and have a clear indication of how the Council will deliver a balanced budget and which services will be prioritised.

2.26 The Council's public promises and high priority areas remain the focus for investment. Non customer-facing support services together with lower priority services and services delivering poor value for money will be the main focus of savings proposals. Working in partnership with others, strategic procurement and delivering services in different ways offer further opportunities to reduce costs.

2.27 Other actions aim to generate additional, sustainable income. Changes to our approach to asset management will be key to this, via plans to share overheads and co-locate with partners.

Timetable

2.28 In order to produce these action plans extensive consultation is required with all stakeholders including members, residents of the District and our partners. This consultation will begin with a workshop with the Executive in July 2010.

Month	Task
Jun-10	Commence work on statutory / discretionary review of services
Jun-10	Commence lobbying with Oxfordshire and Northamptonshire on Concessionary Fares
Jul-10	Executive Workshop
Jul-10	Resident Budget Consultation
Aug-10	Formal Response to DCLG on Concessionary Fares and Settlement
Aug-10	Review work on statutory / discretionary review of services
Aug-10	Develop Action Plans for each MTFS Scenario
Sep-10	Executive Workshop
Sept-10	Budget Guidelines to Executive
Oct-10	MTFS Action Plans to Executive
Nov-10	Local Government Provisional Settlement
Dec-10	Executive receives Draft 1 budget proposals including savings and efficiencies
Jan-11	Local Government Final Settlement
Jan-11	Executive receives Draft 2 budget proposals and MTFS
Feb-11	Full Council approves MTFS, Budget and Council Tax

Consultations

Various consultations with Local Government Association (LGA), Communities and Local Government Office (CLG) and neighbouring authorities.

The scenarios modelled have been discussed and reviewed with the Corporate Management Team as part of the 2010/11 budget process and during meetings in April and May 2010.

Implications

Financial:

Financial Effects: There are no direct financial effects on the Council from this report but the scenarios modelled indicate the potential funding shortfalls that might arise depending on the funding available. In order to ensure that the services can be delivered a robust action plan is required for each scenario.

Comments checked by Karen Muir, Corporate Accountant, 01295 221559.

Legal:

The Council has a statutory duty to deliver a balanced budget and therefore any reductions in funding must be met with reductions in expenditure.

Comments checked by Liz Howlett, Head of Legal and Democratic Services/Monitoring Officer 01295 221686

Risk Management:

The significant risks and assumptions associated with the MTFS forecasts are included within this report. If due consideration is not given to matching scarce financial resources carefully against properly assessed service priorities, the Council may fail in achieving its strategic priorities and in its duty to demonstrate value for money.

Comments checked by Karen Muir, Corporate Accountant, 01295 221559.

Wards Affected

All

Corporate Plan Themes

An Accessible, Value for Money Council

Executive Portfolio

Councillor James Macnamara - Portfolio Holder for Resources

Document Information

Appendix No	Title
Appendix 1	MTFS Scenario Analysis
Background Papers	
2010/11 – 2013/14 Medium Term Financial Strategy (April 2009)	
2010/11 Budget Book	
Cherwell's Sustainable Community Strategy, 'Our District, Our Future'	
Procurement Strategy 2010/11	

MTFS Financial Model	
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