



CABINET

12 OCTOBER 2016

Subject Heading:

The Council's Financial Strategy

Cabinet Member:

Cllr Roger Ramsey

SLT Lead:

Andrew Blake-Herbert
Chief Executive

Report Author and contact details:

Mike Board
Corporate Finance & Strategy Manager
01708 432217
mike.board@onesource.co.uk

Policy context:

The Council is required to approve an annual budget and to establish a financial strategy and this report forms the initial phase of that process.

Financial summary:

This report sets out the process for developing the medium term financial strategy for the Council

Is this a Key Decision?

No

Is this a Strategic Decision?

No

When should this matter be reviewed?

December 2016

Reviewing OSC:

Overview & Scrutiny Board

The subject matter of this report deals with the following Council Objectives

Havering will be clean and its environment will be cared for [x]

People will be safe, in their homes and in the community [x]

Residents will be proud to live in Havering [x]

SUMMARY

This report sets out the Council's Medium Term Financial Strategy to manage the implications of funding reductions and cost pressures over the next three years.

It sets out the process for bridging the funding gap with a view to achieving a balanced two-year budget.

It reviews the cost pressures faced by the Council and updates the financial model as reported to the Council in February 2016 when setting the Council Tax requirement for 2016-17.

The financial strategy has been updated on the assumption that the Government's four year financial settlement will be implemented.

It also explains the process and timescales for identifying further cost savings and income generation proposals that are required to meet the funding gap over the three year cycle.

All proposals will be subject to full and proper consultation, before any final decisions are made.

RECOMMENDATIONS

That Cabinet:

1. **Note** the original and currently projected budget gap and the assumptions upon which these have been based, and the risks associated with them.
2. **Agree** the draft Medium Term Financial Strategy (MTFS), covering the period from 2017/18 to 2019/20, set out in this report.
3. **Note** that there is a range of risks and assumptions made as part of the development of this strategy and that updates will be provided to Cabinet should these vary, in the build-up to Council Tax setting.
4. **Note** that any alternative proposals from Overview & Scrutiny or opposition groups, that would need to be subject to consultation, will need to be subject to a robust review before they can be considered for inclusion in the Council's budget and therefore must be submitted by 10th November prior to the next meeting of Cabinet on 14th December in order to be considered as part of the consultation process.
5. **Note** that a range of corporate strategies may be impacted by the budget strategy and these will need to be updated and approved accordingly.

6. **Review** the initial proposal to maintain a core capital programme of around £4.9m a year subject to a detailed review of available receipts and to a further review of borrowing costs.
7. **Agree** to receive a further report in December to consider progress to date in delivering the 2016/17 budget, developing further proposals for 2017/18 and beyond and providing an update on the prospects for the financial settlement following the Chancellors autumn statement.
8. **Note** the advice of the Section 151 Officer in setting a robust budget.

REPORT DETAIL

1. STRATEGIC APPROACH

- 1.1 In the report to Cabinet in February 2016, the Council set out a financial strategy which balanced the budget for 2016-17 but required further savings of £6.7m to be found in 2017/18 and 2018/19. Further Council Tax increases of 2% per annum (plus a 2% Social care precept) had been assumed in arriving at this figure. It was noted that the forecast savings gap would be significantly higher if a lower Council Tax increase were to be applied.
- 1.2 Given the impact on the Council's budgets of demographic growth, and an ageing population, it is essential that the Council sets out a long-term strategy for bridging the financial gap. This report represents the start of that process.
- 1.3 The first step has been to review the progress to date in delivering the 2016-17 budget. All of the savings identified and agreed need to be fully delivered for the budget strategy to balance. Failure to do so can result in further cost pressures and a requirement to identify the means of funding them.
- 1.4 The second step was to consider and review the impact of cost pressures and corporate assumptions on the MTFS in future years.
- 1.5 The third step is to update any assumptions for the Local Government financial settlement. The four year financial settlement applicable from 2016/17 should provide greater predictability in the level of Government funding. The position will be considered further following the Chancellors Autumn Statement and the annual settlement which is expected to be confirmed in December.
- 1.6 The final step has been to update the financial model in order to produce a revised savings target for the three year period to 2019-20.

2. REVIEW OF 2016-17

- 2.1 The Council approved a balanced budget in 2016-17 as part of its three year MTFS strategy as set out in the Council Tax report approved in February 2016. In establishing the starting point for the consideration of the 2017-18 budget it is necessary to review the latest budget monitoring position for 2016-17 to

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determine whether the Council is on track to deliver its out-turn in line with budget.

- 2.2 The first monitoring report of 2016-17 has indicated a potential in-year overspend against service department budgets of £6.5 million. This does not reflect any allocation from central contingencies, neither does it reflect any alternative proposals which are expected to be developed to alleviate these pressures.

The 2016/17 forecast outturn as reported for period 3 is set out in the table below.

Directorate	Revised Budget	Forecast Outturn	Forecast Outturn Variance
	£'000	£'000	£'000
Public Health	0	635	635
Learning & Achievement	15,917	16,865	948
Children's Services	27,405	28,868	1,463
Safeguarding - Quality and Assurance	1,673	1,729	56
Housing Services	1,874	3,219	1,345
Adult Services	52,992	54,601	1,609
Mental Health	2,909	2,812	(97)
Neighbourhoods	24,572	25,436	864
oneSource Non-Shared	376	141	(235)
Chief Operating Officer	30,720	30,621	(99)
Sub total	158,438	164,927	6,489
Contingency	1,965	1,965	0
Revenue Total	160,403	166,892	6,489
Dedicated Schools Budget	0	0	0
oneSource shared	2,524	2,524	0
Grand Total	162,927	169,416	6,489

- 2.3 The principal variances underlying the period 3 forecast rest in Housing, Children's and Adults Services. Further analysis of the causes of the variances is being undertaken by Senior Management but Cabinet will be aware of the continued pressures of demographic growth in these areas. There are also risks associated with the timing and delivery of savings proposals agreed as part of the 2016/17 budget strategy. Some of these issues may be mitigated by corporate measures but the risk of overspending has increased significantly and actions will be required to prevent the financial strategy from being compromised.
- 2.4 The overall budget includes a general contingency of £2 million. This was established to ensure that the Council's budget is robust, and able to provide financial stability to enable adverse in-year variances to be overcome. The level of this budget is re-assessed annually as part of the budget-setting process. In accordance with previous practice any allocations from contingency will not be considered until all other measures have been explored. This contingency is designed to enable the Council to resolve any in-year issues that cannot otherwise be contained within approved budgets. It is not however available to fund permanent, on-going changes; these need to be resolved as part of the formal budget-setting process. Cabinet will also be aware that the

contingency is planned to be reduced to £1 million in 2018/19 as set out in the MTFS.

- 2.5 The 2016/17 budget also includes a number of corporate provisions which could if required be used to meet the additional pressures arising during 2016/17. Crucially, these sums are planned to be removed from the base budget in 2017/18 and later years as part of the draft MTFS. These adjustments are included in the table at paragraph 4 below.
- 2.6 Those service departments currently showing overspends are working on action plans to review in-year performance in order to identify steps which can be taken to reduce the financial impact of these budgetary pressures in the current period and to bring spending back in line with budget over the medium term cycle. These will be available for the period 6 monitor. At this stage the assumption is that these plans will be deliverable, so there is no requirement to adjust the previous budget strategy assumptions.

3. PROSPECTS FOR THE LOCAL GOVERNMENT FINANCIAL SETTLEMENT

- 3.1 At its meeting of 14th September the Council agreed to accept the Government's offer of a four year financial settlement to provide greater certainty over the level of Council funding and will make financial planning easier to manage over this period.
- 3.2 The Government is expected to announce the Local Government Financial Settlement in December 2016 which should be in line with the position established during the 2016/17 announcements. The Government has indicated that changes will only be made in exceptional circumstances. The outcome of the settlement will be reported to Cabinet in January 2017 and will also be reflected in the final budget report to Council.
- 3.3 There are currently three major consultation documents due to be returned shortly. Further details on the responses will be circulated to Cabinet in due course. These consultations are:
 - 3.3.1 Self Sufficient Local Government : 100% Business Rate Retention:

The Government are seeking views on ways in which it could implement a system under which Local Government retains 100% of the Business Rates it collects. Under such a system additional burdens would be transferred from Central to Local Government. The consultation closes on 26th September and a copy of the response will be circulated in advance of the meeting.
 - 3.3.2 Fairer Funding Review

This consultation sits alongside the Business Rates Review and gives the Council the opportunity to comment more widely on Local Government funding. This consultation also closes on 26th September and a copy of the response will also be made available to members.
 - 3.3.3 Local Government Financial Settlement 2017/18

The annual consultation on the annual financial settlement closes on 28th October 2016. Councils have until 14th October to respond to the offer of a four

year financial settlement. Havering will be accepting the offer as previously approved.

4. THE MTFS MODEL 2017-18 and 2018-19

4.1 The MTFS as approved at Cabinet in February 2016 indicated that a budget deficit would arise in 2017/18 and 2018/19 and that further action would be required to balance the budget in each of those years.

4.2 The model has now been updated to reflect a more accurate estimate of known pressures facing the Council and the revised assumptions on the level of Council Tax increases discussed at paragraph 6 below. For the purposes of financial planning it is assumed that the 2016-17 out-turn will be brought back in line with budget (or that any service overspending will be met from contingency). It is also assumed that these in year pressures will not give rise to on-going pressures requiring additional measures to be taken as part of the MTFS process. The matter will be reported further at the December cabinet meeting outlining progress to date and any amendments required to the strategy.

	17/18 £000's	18/19 £000's	Total £000's
	£'m	£'m	£'m
Budget Gap as reported Council Feb 2016	2.432	4.265	6.697
(a) Re-phasing of pressures	1.050	(2.217)	(1.167)
(b) Re-phasing of Savings options	1.500	2.000	3.500
(c) Reduction in Council Tax increase	0.915	1.915	2.830
d) Transitional grant	(1.416)	0.000	(1.416)
Revised Budget Gap	4.481	5.963	10.444
(e) Corporate contingencies and reserves	(3.373)	(4.859)	(8.232)
(f) Star Chamber options	(0.758)	(0.854)	(1.612)
Remaining Budget Gap	0.350	0.250	0.600

4.3 The following adjustments have been made to the strategy since February 2016 (as reflected in the above table). The causes of these adjustments are broadly as follows:

- a) The timing of budgetary pressures, principally the delay in the expectation of an increase in interest rates.
- b) The lead in time for the implementation of approved savings proposals.
- c) Revised assumptions on the level of Council Tax increase.
- d) The inclusion of transitional grant received after the budget was approved (and compensating for the use of reserves)
- e) The removal of corporate contingencies, grants and provisions from the base budget.
- f) Draft savings and income generation proposals arising from the Star Chamber process.

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- 4.4. Cabinet will note that there is a residual gap of £0.6m for which additional savings will be required. These will be considered and reported alongside the draft Star Chamber proposals later in the budget development cycle.

5. IMPLICATIONS FOR COUNCIL TAX

- 5.1 In setting the 2016-17 budget, and given the scale of cost reductions required the Council approved an increase in Council Tax of 1.99% plus a 2% Social Care precept. Further increases in Council Tax were proposed at this level for the remaining two years of the strategy as approved by Council in February 2016.
- 5.2 Mindful of the impact of cumulative Council Tax increases on residents the level of increase included within the revised MTS has been reduced to the following levels.
- 1% in 2017/18 (plus 2% social Care precept)
 - 0% in 2018/19 (plus 2% social Care precept)
 - 2% in 2019/20 (plus 2% social Care precept)
- 5.3 The latest version of the model incorporates these options. Further consideration of the proposed increases will be included in the February report. Cabinet will be aware that additional savings proposals will be needed to compensate for any shortfall in revenue arising from further reductions in Council Tax income.
- 5.4 Cabinet will also be mindful that increases of 2% or more will almost certainly be subject to approval through a public referendum.

6. CONSULTATION AND ALTERNATIVE BUDGET PROPOSALS

- 6.1 The additional savings and income generation proposals will be considered by Cabinet on 14th December along with an update to the MTFs strategy. These proposals may subsequently be considered by Overview & Scrutiny, consultation prior to inclusion in the draft MTFs and Council Tax setting report for 2017/18.
- 6.2 Given the overall scale of the budget gap should any of the proposals be rejected, either at the joint Overview and Scrutiny meeting or Cabinet meeting, alternative proposals will need to be put forward

7. EXPENDITURE AND PERFORMANCE

- 7.1 As reported to Cabinet in October 2015 LG Futures carried out an analysis of Council spending based upon statutory Government returns relating to the 2015/16 budget. In doing so they were able to make comparisons of Havering's expenditure against two distinct groups:
- Nearest Neighbour Group (NN) – 16 authorities with similar demographic and socio-economic characteristics (mainly outer London boroughs)
 - Comparable English Authorities (CEA) Group – 123 authorities with similar functions and responsibilities.

- 7.2. The detailed report provided an analysis of Havering's budgets as compared with similar authorities. Havering's lower spending is a reflection of national funding restrictions which have been discussed at some length in previous reports. The report however, enabled comparisons to be made at service level and most interestingly highlights areas of service expenditure which appear higher than that of our comparable authorities.
- 7.3 LG Futures have recently updated the comparative data based upon the 2016/17 budgets and the following highlights are worthy of mention.
- Overall Havering's total unit costs are 2.5% lower than its NN average (11.9% lower in 2014/15) and 17.9% below the CEA average (21% lower in 2014/15).
 - Adults and Children's Social Care account for over 50% of budgeted expenditure and therefore have the greatest influence on overall unit costs.
 - Havering has lower unit costs in Adult Social care but higher than average unit costs for Children's Social Care.
 - For most other services Havering's unit costs were below the NN and CEA average.
 - For 2016/17 Havering's total unit costs were 9th lowest of 16 within its NN group and 109th lowest out of 123 of its CEA group.
 - Its unit costs for Children's Social Care are second highest of its NN group and 17th highest of its CEA group.
 - Its unit costs for Highways and Transport are 10th out of 16 within its NN group and 24th highest of its CEA group.
- 7.4 These findings may be of help at a time when the Council is facing increasing cost pressures and is seeking to make additional budget savings over the term of its MTFS.

8. SPECIFIC BUDGET ISSUES

8.1 There are a small number of specific issues which have a significant impact on the budget, which are addressed below. These have been highlighted in previous reports to Cabinet, but are raised here so Cabinet is aware of them in the context of the development of the future budget strategy.

8.2 Freedom Pass

The Council's current contribution to the concessionary fares scheme stands at £8.2m. Havering has seen lower rises than other boroughs, due to our comparative usage figures, and this is reflected in the proposed future strategy. An increase of £300k per year is included in the model. There remains a risk that a significant rise in usage could affect Havering's contribution, particularly now TfL has become responsible for more stations.

8.3 Levies

There are a number of levies raised on Havering, the largest of which is East London Waste Authority (ELWA). The overall levies budget is £14.4m, of which the biggest element, ELWA, is around £13.6m. The ELWA levy is predominantly made up of the Shanks contract. The budget strategy is based

on the most recent forward plan for the Authority. Going forward there are risks associated with waste tonnages, as the levy reflects these, so a disproportionate rise will affect the distribution between the constituent Councils.

8.4 Specific Grants

The Council still receives a number of specific grants from Central Government which may be earmarked for specific purposes. In recent years the number of these grants has reduced or in some cases rolled into mainstream grant funding and reduced accordingly. The remaining specific grants include the Public Health Grant and Educational Services Grant (ESG) both of which have been subject to reductions in recent years. Where such grant streams have been reduced or are to be reduced it is expected that corresponding service spending reductions will be required.

9 IMPACT ON COUNCIL STRATEGIES

9.1 The budget strategy and the savings proposals to be considered by Cabinet at the October meeting may impact on a number of strategies previously agreed by the Council, through either Cabinet or Cabinet member delegation. On the assumption that Cabinet agrees the proposals, after considering the views of the joint Overview & Scrutiny Committees, these proposals will be subject to a formal consultation process. Depending upon the nature of the approved savings proposals it may be necessary to undertake a concurrent review of any strategies affected and to submit these for approval, and any necessary consultation process, over the coming months. Cabinet is asked to note this.

10. CAPITAL PROGRAMME

10.1 Based upon the approved programme for 2016/17 an indicative programme for 2017/18 would be as follows:

Description	£000's
Cemeteries	160
Parks,	510
Libraries	145
Leisure	185
Street Environment	2,000
Protection of Assets and Health and Safety	500
IT Infrastructure	1,000
Regeneration	100
Disabled Facilities Grant (Council element)	300
Sub total	4,900
Contingency	2,000
Grand total	6,900

10.2 The current core programme is funded exclusively from capital receipts generated from the disposal of assets. The projected budget gap makes no allowance for any cost arising from prudential borrowing. Should there be insufficient receipts to finance capital spend, it would either need to be reduced to fit within the available receipts, or funded through borrowing; the latter

measure would then need to be taken into account as part of the overall budget strategy, as it would increase the existing budget gap.

- 10.3 A further review of available receipts is currently underway and once completed, an assessment will be taken of the overall sum available. From this, proposals for a long term core capital programme will be drawn up for consideration as part of the formal budget setting cycle during January and February. This will include detailed schemes within each element of the core programme. As part of this, the potential to generate additional receipts from the disposal of surplus properties will be identified, should this be needed to continue to deliver a similar programme in future years.
- 10.4 A provision of £100m for Regeneration and Development projects to be funded from prudential borrowing was also included in the 2016/17 Capital programme. Individual scheme approval is required before sums are allocated from this provision. The Treasury management strategy assumes a cash outflow of £20m per annum over five years although the sum may be allocated earlier in the cycle if required.
- 10.5 Given the historically low levels of interest rates and the diminishing levels of capital receipts available to fund capital schemes it may be prudent to consider the use of borrowing. Further consideration to this matter and to the level of further capital contingency will be included in the January cabinet report.
- 10.6 At this stage, Cabinet is asked to agree in principle to an overall core annual programme of £4.9m for 2017/18. This will enable officers to draw up detailed schemes for later in the budget setting cycle.

11. BUDGET ROBUSTNESS

- 11.1 The Council is required to set a balanced budget, taking into account a range of factors, including appropriate consultation and equality impact assessments. A key factor is to ensure that Cabinet are made aware of the advice of the Council's Chief Finance Officer (CFO) in making decisions relating to the Council's budget.
- 11.2 The Local Government Act 2003 sets out requirements in respect of Financial Administration, and in particular to the robustness of the budget and the adequacy of General Fund reserves. The Act requires the CFO to report to an authority when it is making the statutory calculations required to determine its Council tax or precept. The Act also suggests the advice should be given prior to the formal statutory calculation. This advice has therefore been given to both Cabinet in formulating proposals and to members of Overview and Scrutiny in considering the proposals, as part of previous budget setting cycles.
- 11.3 The advice of the CFO was set out at some length in the report to Cabinet in February 2016, in Appendix H of that report. Cabinet is asked to be mindful of this advice in reviewing proposals as they are brought forward for consideration during the budget development process when these are subsequently scrutinised by the Overview & Scrutiny Committee, and in then considering any alternative proposals. In particular, the need to set a balanced budget within the context of a medium term financial strategy is a prime responsibility for the CFO.

REASONS AND OPTIONS

Reasons for the decision:

It is essential that the Council's financial strategy takes due account of Government plans and any other material factors where these are likely to have an impact on the Council's financial position. This report sets out the process for developing the Council's budget strategy for the next three years and reflects the expected continued Government approach of reduced levels of funding.

Other options considered:

None. The Constitution requires this as a step towards setting the Council's budget.

IMPLICATIONS AND RISKS

Financial implications and risks:

The Council's budget process will ensure that financial implications and risks are fully considered. There are continuing risks with the potential impact on funding arising from both the Budget and Comprehensive Spending Review (CSR) announcements, as highlighted in both this and the previous report to Cabinet. The steps already taken by the Council should mitigate this, but it is evident that a longer term approach now needs to be considered, as the potential scale of the future budget gap could prove to be even bigger than the gap the Council is currently addressing.

There are considerable risks in the medium to longer term, with the continuing economic uncertainty as well as the likely impact of further funding changes. There are also considerable uncertainties stemming from the Care Act and the Children & Families Act, and although the Government has given an undertaking that new burdens will be funded, it remains to be seen what effect these will have locally and whether there will be any adverse financial impact. The Council therefore needs to maintain a prudent approach over its financial management and the budget setting process. It is essential that the Council puts a strategy in place to deal with the further reductions in Government funding.

The Council is required to set a balanced budget and the proposals that are made as part of the budget development process will need to be robustly reviewed, challenged and scrutinised, and consulted on wherever appropriate. The advice of the Section 151 Officer must be taken due account of within the budget setting process and that applies to all budget proposals, whenever they are put forward. This will mean a much more robust process will have to be applied to any alternative proposals put forward to those being made by the Administration; this could potentially necessitate formal consultation with the local community. All such proposals will be reviewed by the Section 151 Officer before they can be considered by Cabinet and Council.

Legal implications and risks:

The Council is subject to a number of duties in relation to revenue, capital and procurement. For instance, as a Best Value Authority the Council is under a duty to *“make arrangements to secure continuous improvement in the way in which its functions are exercised, having regard to a combination of economy, efficiency and effectiveness.”* s 3 Local Government Finance Act 1999. The Council is also under an implied duty to set a balanced budget. Beyond these there are no apparent specific legal risks in adopting the recommendations set out in the report, providing appropriate consultation is carried out at all stages.

Human Resources implications and risks:

The Council continues to work closely with its staff and with Trades Unions to ensure that the effects on staff of the savings required have been managed in an efficient and compassionate manner.

All savings proposals or changes to the funding regime that impact on staff numbers, will be managed in accordance with both statutory requirements and the Council's Managing Organisational Change & Redundancy policy and associated guidance.

Equalities implications and risks:

This report sets out the Council's medium term financial strategy to manage the implications of funding reductions and cost pressures over the next three years, so that it is able to operate with a balanced budget and ensure the continued running of the most valued, and statutory, public services.

The Council faces significant challenges in achieving a balanced budget, not only in terms of funding reductions, but also in terms of the rising demand for services, brought about by Havering's increasing older demographic, as well as major national policy pressures such as the implications of the Care Act.

Proposals are currently being developed to bridge the funding gap and will be considered by Cabinet in October. Where proposals affect staff, service users, or indeed the wider population, they will need to be thoroughly analysed for disproportionate negative impact, with mitigating actions identified to minimise any negative impact. All proposals will be subject to consultation with Councillors, staff, service users and the general public as appropriate before any final decisions are made.

Other Risks:

There are no particular other risks arising, other than a very short timescale to properly analyse the LGFS announcements whenever they eventually occur. This is being planned for but much of the detail will have to await the final announcements and publication.

BACKGROUND PAPERS

There are none.