

## Financial Strategy 2006/07

### Head of Financial Services

**Summary:** The Council faces a challenging budget setting process for 2006/07. A number of cost pressures which have been reported to Cabinet previously are coming to fruition, which make it necessary to reconsider the base budget and potentially redetermine priorities.

This view is based on range of assumptions in an uncertain climate, with anticipated poor government grant allocations. There is also the revaluation which will have a significant impact on council tax bandings effective from 2007.

The capital programme also requires careful consideration, as the level of resources to fund future schemes will reduce, as a combination of specifically funded schemes (eg Sewage Treatment Plants), government grants (eg DEFRA, IEG) and Right to Buy receipts all reducing. This will place an increased emphasis on the need to produce business cases with a financial return.

**Conclusions:** The Medium Term Plan and Capital Strategy both look to three year horizons. It is critical that with such changes anticipated that the Councils financial position and strategy is sound and viable, so as to not restrict the continuing improvements in performance.

**Recommendations:** It is recommended that Cabinet provides guidance to officers in the approach to determine a balanced budget for the three year Medium Term Plan and the Capital Strategy.

Cabinet member(s):	Ward(s) affected:
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## 1. Introduction

- 1.1. The purpose of this report is set the framework for developing the revenue and capital budgets for FY 2006/07 and beyond. It makes a number of assumptions so that an outline position can be established at this early stage, enabling Management Team to consider changes to resource allocations as a result.

- 1.2. Looking back to the budget preparation process for FY 2005/06, there were a number of cost pressures which were incorporated into the Medium Term Plan approved by Cabinet and Council in February 2005. These were:
- The valuation of the superannuation fund as at 31 March 2004 identified an increased contribution of £480,000 per annum to redress over a period of some 20 years. Cabinet agreed to phase in this over a six year period, with an increase of £80,000 per annum falling on the budget. Cabinet will be aware that with the proposal to revoke the changes to the pension scheme in April 2005, there are no proposals yet to determine how any increased deficit would be funded.
  - The roll out of the Twin-Bin scheme across the district has been funded in part from DEFRA grant. This grant covered some capital and revenue costs incurred in FY 2004/05 and 2005/06. This funding ceases on 31 March 2006 and it is estimated that the increased cost which will fall on the budget will be £211,000.
  - The successful achievement of Planning Delivery Grant in FY 2004/05 and FY 2005/06 has been used to fund a combination of ongoing (predominantly staff costs) and one-off expenditure (eg consultants). The national Planning Delivery Grant allocation is £135 million in 2006/07 (£170 million in 2005/06) and the ongoing staff costs approved by Cabinet total £273,000. Should the Council be successful in obtaining the same proportion of the national allocation in 2006/07 as it did in 2005/06 then it is predicted that Planning Delivery Grant will cover these costs. But there is a risk in this assumption.
  - The Gershon agenda requires authorities to achieve efficiency savings of 2.5% per annum. The Efficiency Plan for 2005/06 shows where savings can be made in each of the next three years. The realisation of these savings will be necessary both to deliver the Efficiency Plan and to reallocate resources through this budget setting process.
  - Government grant (Revenue Support Grant and redistributed business rates) increased by 7.4% in FY 2005/06. Cabinet was advised that such an increase should not be anticipated for future years, and a projection of a 2.5% increase was included in the medium term plan.
- 1.3. There are also structural budget pressures at present. The outturn in 2003/04 showed a service underspend of £888,000, partially offset by capital accounting adjustments of £123,000. The outturn position for FY 2004/05 shows services breaking even, with only one offs (eg carry forward of previous year underspends, Planning Delivery Grant and interest on investments) providing the net underspend. This suggests that expenditure levels are in line with budgets in FY 2004/05, or put another way, the ability to enhance performance is being restricted by budget availability.
- 1.4. Management Team took some difficult decisions during the latter part of FY 2004/05 in managing a more cautious approach to recruitment was correct. Furthermore, Heads of Service have been asked to review all of their staffing levels vis a vis budgets before vacancies can be filled.
- 1.5. The Council's budget depends on interest from investments as a source of income (the income in 2004/05 was just below £1.5 million). The base budget assumes an interest rate of 4.5%. Rates are predicted to fall in the coming months, and there are forecasts which show interest rates falling to below 4.25%

by January 2006. At present the assumption that an average interest rate of 4.5% could be achieved across all investments, but this is coming into question, and the position will be clearer later in the year.

- 1.6. Finally, the full impact of the loss of Service Level Agreements (SLAs) with SNHP have yet to be fully reflected in the current year's budget. There have been some reductions in direct costs as a result, but there has not been a reduction in overheads. The 2005/06 base budget provides for £225,000 increased costs falling on the General Fund, on the assumption that some, but not all, SLAs would be lost. The outcome of the discussions with SNHP is that the vast majority of SLAs have now ceased, and initial estimates put the additional cost to the General Fund in excess of £500,000, an additional cost pressure of more than £275,000 compared to the 2005/06 base budget. This will have consequences on the current and future years costs.

## **2. Corporate Plan**

- 2.1. The Corporate Plan will show priority areas for service improvement, and it is recommended that should any growth be affordable, that it is driven by that plan. It is not considered that the Corporate Plan will highlight specific areas for budget savings.

## **3. National Changes**

- 3.1. A full revaluation of properties and a potential revised banding system will take effect from April 2007. The potential to amend the bandings and proportions each band pays in council tax is likely to lead to a greater volatility in council tax increases in 2007 and in the immediate years following. The government has stated that it does intend to use the revaluation to shift taxation onto the council tax system. But there is the risk that should increases in values in south Norfolk be greater than the national average, that council taxpayers could well see an increase in their bills as a result. The experience in Wales is that a ninth band was added at the higher end (values in excess of £424,000). The valuation changes varied with 58% of properties remaining in the same band with 8% reducing. It is suggested in the national press that the overall impact was to increase the tax burden across Wales by 9.1%.
- 3.2. The government grant allocations are subject to a complex formula. Based on the previous formula this Council had some government funding scaled back to fund those councils on the floor. In fact, this Council had its grant reduced by £389,963 (£513,848 in 2004/05) in order to fund authorities facing an increase below the floor of 2.5%. Cabinet will note that the gap is reducing.
- 3.3. The likelihood that this Council receives a favourable settlement or otherwise is subject to the Review and the formula to be used. It has therefore been assumed for financial planning purposes that a minimum level of grant increase, of 2.5%, would be prudent. It is not clear whether any government grant will be abated by the efficiency savings achieved.

## **4. Medium Term Plan**

- 4.1. The Medium Term Plan sets out the 3 year revenue budget forecast (shown at appendix A). At the most recent update the average council tax increase over

that period is in excess of 5%. However, this forecast does not allow for any service growth or reductions. Nor does it allow for any savings to arise from the Best Value Review of Support Services. It is recommended that an assumed saving of £200,000 could be considered appropriate.

- 4.2. The Medium Term Plan suggests that should members wish to set at council tax increase at or below 5%, that it will be necessary to reset the cost base. Bearing in mind the level of expenditure is now in line with budgets, any proposals to reduce budgets will inevitably impact on service quality, unless efficiencies can be identified. Work on the Best Value Review of Support Services and the Gershon agenda continues, and it is assumed that these two issues identify savings of £346,000 in 2006/07. This would enable a council tax increase to be set at 5% without any service growth at all. But it is questionable whether the budget deficit could be closed by these two issues alone. It will therefore be necessary to prioritise some areas of expenditure where efficiencies and/or budget reductions are made.
- 4.3. All of these projections are based on the use of Revenue Reserves at £150,000 per annum. The Financial Strategy assumes that the use of reserves are affordable for the period of the Medium Term Plan (ie 2006/07 to 2008/09). There are sufficient reserves to satisfy this. There is the potential to increase the use of reserves in the short-term if there is certainty of reduced dependency in the longer term (ie invest to save).
- 4.4. The level of redefining the base budget in putting together a balanced budget depends on levels of government grant and the council tax to be approved by full Council. Assuming that Cabinet will wish to recommend to full Council a council tax increase of 5% or under, the table below sets out the budget deficit (based on current assumptions) which needs to be closed on each scenario:

Council Tax Increase	Forecast Budget Deficit (£000)
0%	653
1%	601
2%	549
3%	497
4%	445
5%	393

- 4.5. Cabinet will note that the deficit referred to above would be reduced by £389,963 (para 3.2 above) if the Council did not have its Revenue Support Grant “scaled back. The budget forecasts are regularly discussed at Management Team, and a suggested way forward has been agreed, which assesses a range of issues, which can be summarised as follows:

- a) The agreement to achieve lower and bottom quartile in low priority BVPIs may be an opportunity, but these do not cover all aspects of council business.
  - b) Review maintenance costs of existing assets, principally buildings but could include ICT
  - c) Review the resource levels in areas where related capital schemes will be significantly reduced in future years.
  - d) Focus reducing capital resources on schemes which maintain the value of existing assets or have a business case with a financial return.
  - e) The BVR of Support Services will focus on administration functions and/or reducing management overheads.
  - f) Focus on raising income levels, above the normal inflationary increases (eg car parks, leisure).
  - g) Joint working or outsourcing.
  - h) Focus on services which no longer have SLAs with SNHP, and to a lesser extent the Building Control Partnership.
- 4.6. Rather than the traditional approach of seeking savings and growth bids on a service by service basis, Management Team considers that the financial pressures the Council faces, together with the fact that services are being provided at budget (ie there is no spare capacity), requires a fundamental corporate review of resources in line with priorities. This work will be undertaken during the summer and brought back to Cabinet once proposals have been tested.
- 4.7. If this process is not successful, the alternative is to make across the board savings, for example by freezing all existing budgets from 2005/06 into 2006/07, including both pay and non-pay budgets. This would impact on all services equally, and would mean that the level of vacancies services run with would increase, and would ultimately be a less than ideal way of managing such critical services.
- 4.8. The Audit Commission has recently issued the guidance and areas of focus in the new "Use of Resources" element of CPA. This will be a challenging piece of work, and parts of it will influence the financial standing and planning arrangements in place. This work will take place during the summer.

## **5. Capital Programme.**

- 5.1. The report elsewhere on the agenda sought Cabinet's approval to slippage requests. Assuming these were approved, the capital programme in 2005/06 would then be in excess of £10 million, with a projected programme in future years at around £3 million per annum. This clearly brings into question the capacity of the Council to deliver such a challenging programme, and all project managers have been asked to consider a more balanced programme which sees a more even spread over the next three to four years which reflects capacity issues. Once this work is complete, the capital programme will be revised and presented to Cabinet for approval.
- 5.2. The Capital Strategy for 2006/07 to 2008/09 will be presented to Cabinet in November, following Cabinet consideration of the IEG Statement and the Asset

Management Plan. The officer working group developing the Balancing Housing Markets also has the key role to play. These three strategies drive the formulation of the capital programme, with the Capital Strategy acting as the strategic overview.

- 5.3. With regard to the capital programme, Cabinet approved a three year capital programme in February 2004 covering the FYs 2004/05 to 2006/07. This was an affordable programme, although there was a minor funding gap towards the end of the third year. It is proposed that with the significant change in the resources available to support the capital programme (a revised capital funding statement is attached at appendix B to this report), that a new three year Capital Strategy is formulated to cover 2006/07 to 2008/09.
- 5.4. The resources will be significantly reduced due to the following reasons:
- Right to Buys continue to decline. It is projected that a capital receipt of £1.6 million be available in 2006/07.
  - The VAT shelter will be delivering a slower pace of capital receipts than had originally been predicted. The original assumption of an annual receipt of £0.5 million has been adjusted to £0.3 million per annum.
  - Capital grants from DEFRA and IEG are anticipated to cease after 2005/06. These account for £0.8 million of funding in the current financial year.
- 5.5. At headline figures, excluding the affordable housing schemes which will be added should further housing land sales be made, the capital resources are projected to be approximately £9 million over the three year period. To put this into context, the resources available for the 2004/05 to 2006/07 capital programme totalled £20 million. In order to prioritise capital schemes and projects for the Capital Strategy, it is suggested that schemes which are included in the capital programme will:
- a) focus on maintaining and improving on existing assets (indeed some pressures have already been highlighted through the Asset Management Plan), and
  - b) the ability to invest in new assets will depend on a business case showing a rate of return on that investment.

## **6. Timetable**

- 6.1. The outline timetable is as follows:

July- September	The restatement of the 2005/06 revenue and capital budgets  Management Team considers cost base and priorities, identifying efficiencies and/ or reductions  Management Team develop service plans, in support of the corporate plan and the Gershon report
October- December	PDPs, Older People's Forum, SN Youth Action, Scrutiny and Cabinet consider service plans
November	Cabinet approves 2005/06 budget revisions

December	Medium Term Plan update, service plans, feedback from PDPs and Scrutiny, provisional settlement announced
February	Formal budget and council tax approval

## **7. Conclusion**

- 7.1. Cabinet is requested to consider the framework and advise officers of any specific issues which should drive the formulation of revenue and capital budgets.