

Report to: **Executive**
Date: **19 July 2018**
Title: **Medium Term Financial Position for 2019/20 onwards**
Portfolio Area: **Cllr R Tucker – Annual Budget**
Wards Affected: **All**

Relevant Scrutiny Committee: Joint Development Management Committee and Overview and Scrutiny Panel

Urgent Decision: **N** Approval and clearance obtained: **Y**

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Recommendations:

It is RECOMMENDED that the Executive:

- i) Notes the forecast budget gap for 2019/20 of £0.995m and the position for future years**
- ii) Notes the options identified and timescales for closing the budget gap in 2019/20 and in future years, to achieve long term financial sustainability**
- iii) Agrees maintaining the current Council policy on the minimum level of the Unearmarked Revenue Reserves being £1,500,000 as per Section 10.**

1. Executive summary

- 1.1** The Council's Medium Term Financial Position (MTFP) is based on a financial forecast over a rolling five year timeframe to 2023/24.

- 1.2 The Council, along with other local authorities, has faced unprecedented reductions in Government funding since the Comprehensive Spending Review 2010.
- 1.3 Between 2009/10 and 2019/20, the Council's Core Government funding has reduced by £4 million.
- 1.4 South Hams has continued to work in partnership with West Devon Borough Council which has allowed South Hams District Council to achieve annual savings of £3.9 million and more importantly protect all statutory front line services.
- 1.5 Between both Councils the annual shared services savings being achieved are over £6 million. However, the Councils continue to face considerable financial challenges as a result of uncertainty in the wider economy and constraints on public sector spending.
- 1.6 ***South Hams District Council is currently forecasting a £0.995m budget gap in 2019/20.*** It is important to note that this is a snapshot (a position statement) in July 18 and future Member decisions on the budget strategy will inform future figures within the Medium Term Financial Strategy (MTFS), which will be presented to Members at the Executive meeting on 13th September 2018. The Overview and Scrutiny Panel will consider the MTFS at their meeting on 6th September.
- 1.7 There has been an increase in the budget gap for 2019/20 of approximately £350,000 from the position identified at February 2018. This is due to the additional cost pressures which have been identified for 2019/20 onwards as set out in Sections 5.6 to 5.10.
- 1.8 This report is the starting point for developing a meaningful five year strategy that sets out the strategic intention for all of the different strands of funding available to the Council. The Council will then be able to rely on this to inform future decisions.

2 THE FOUR YEAR SETTLEMENT FUNDING OFFER

- 2.1 During 2016/17 the Government offered Local Authorities the opportunity to apply for a four year agreed funding settlement, subject to the production of an efficiency plan. The Council applied and was accepted for the four year agreement. From 2018/19 onwards, the Council has received no Government funding (Revenue Support Grant) and the Council will need to be self-sufficient. Although the four year settlement offered no Revenue Support Grant, it did guarantee the Council its allocations of Rural Services Delivery Grant over the four year period, which equated to £0.33m in 2019/20.

- 2.2 District Councils such as South Hams have also suffered a large reduction in their New Homes Bonus funding (£0.5 million in 17/18) due to the number of years payments are being reduced, from six years to five years in 17/18 and to four years from 18/19 onwards. The funding being released is to contribute towards adult social care costs, a function carried out by Unitary and County Councils.
- 2.3 Between 2009/10 and 2019/20 the Council's Core Government funding will have reduced by £4 million annually.

3 ASSUMPTIONS FOR FINANCIAL MODELLING PURPOSES

- 3.1 The National Employers made a final pay offer covering 1 April 2018 to 31 March 2020. The majority of employees (those on salaries starting at £19,430 p.a.) have received an uplift of 2% on 1/4/18 and a further 2% on 1/4/19, with those on lower salaries receiving higher increases. The cost of this was £255,000 in 2018/19 and a further £280,000 in 2019/20. This has been reflected in Appendix A. The Medium Term Financial Position is not an expression of Council Policy on pay awards, but a means of ensuring an appropriate provision is made as part of the overall financial planning of the Council.
- 3.2 The report assumes inflation will run at 2.5% over the five year period. The Consumer Prices Index (CPI) was 2.4% in April 2018.
- 3.3 The Medium Term Financial Position has included a cost pressure of £220,000 for Inflation and increases on Goods and Services. The main items are:-
- £80,000 – Staff salary increments
 - £40,000 – Business Rates increases (Revaluation 2017/18 onwards)
 - £30,000 – Utilities inflation
 - £20,000 – Fuel inflation
- An amount of £50,000 is to fund a 2.5% uplift on other expenditure budgets (£2 million).
- 3.4 The predicted interest rate forecast from our treasury management advisors, Link Services, is that interest rates will remain at 0.5% up to November 2018 and then in November 2018 the base rate is predicted to rise to 0.75%. By December 2020 the bank base rate is predicted to increase to 1.5%.
- 3.5 An increase in council tax of the higher of £5 or 2.99% for the next five years has been modelled for council tax purposes. This would equate to a Band D council tax for South Hams of £165.42 in 2019/20 as shown in Appendix B and equates to a council tax increase of 3.1%.

- 3.6 It has been assumed that the number of properties within the District will increase by 450 per annum from 2019/20 to 2023/24 – this is an increase of approximately 1.2% - the Council had 37,851.93 Band D equivalent properties in 2018/19. These additional properties have been used to calculate the amount of additional Council Tax and also the potential for New Homes Bonus. The Tax Base for 2018/19 has been confirmed at 37,851.93 (this was an increase of 472.31 Band D properties from the 2017/18 position).

4. BUSINESS RATES AND COUNCIL TAX

- 4.1 **Retained Business Rates** - The Government introduced the Business Rates Retention system from April 2013. There is a risk of volatility in the system because Councils are exposed to any loss of income if businesses go into decline.
- 4.2 Of the Business Rates collected of £29.8 million, the Council currently retains approximately 6p in every £1 to run our services.

Self-sufficient local government: Business Rates Retention of growth above the business rates baseline

- 4.3 The Secretary of State has announced in December 2017 that local business rates retention of business rates growth would move from 50% to 75% in 2020/21.
- 4.4 **Business Rates Pilot status for 2018/19**
Devon was successful in achieving Business Rates Pilot status for 2018-19 and the pilot began on 1st April 2018. Financial modelling shows that the Devon business rates pool could benefit by somewhere in the region of between £10m to £16.9m by becoming a pilot in 2018/19. The recent modelling shows that South Hams could benefit by £0.5 million, depending on business rates growth estimates. A pilot gain of £575,000 has been modelled for 2018-19. As part of a Pilot, South Hams would receive 40% of all business rates growth above the baseline in 2018-19 (as opposed to 20% outside of the Pool or 22% inside the Pool).
- 4.5 This is one-off additional revenue money for the year of the pilot only (2018/19). The bid set out how pilot status for Devon would meet the principles of higher levels of investment in economic regeneration in Devon, assisting financial sustainability for the District Councils and support for Upper Tier Councils with the growing financial cost pressures of areas such as adult social care and children's services.

- 4.6 Following the recommendations of the Joint Development Management Committee and Overview and Scrutiny Panel on 18th January, £100,000 of the pilot gain (the element that the Council would normally receive in a pooling gain) is being used to fund the revenue base budget in 2018/19, with the remainder (£475,000 of the pilot gain), being transferred into an Economic Regeneration Projects Earmarked Reserve, to meet the primary aims of the Pilot bid which are to achieve higher levels of investment in economic regeneration in Devon and encourage further business rates growth. There will be a further opportunity for Councils to bid for pilot status in 2019-20 and further details of this will be issued by the Government. The Council is awaiting details of the bidding process for Year 2 Pilot status.

Tariff/Top Up Adjustment in 2019/20 (negative RSG)

- 4.7 The Tariff/Top Up Adjustment is an amount in 2019/20 which increases an authority's tariff. It is applied where cuts to a Council's Settlement Funding Assessment (SFA) cannot be achieved through further cuts to the Revenue Support Grant (RSG), as the RSG is already zero.

In effect the Tariff/Top Up Adjustment is negative Revenue Support Grant (RSG). Settlement Funding Assessment is the income received by local authorities in the form of (i) Revenue Support Grant from Central Government and (ii) a share of business rates retained locally.

Negative Revenue Support Grant (negative RSG)

- 4.8 In the Local Government Finance Settlement, the Government has said that a consultation will take place in 2018 regarding the current £153million in negative RSG that remains in the 2019/20 funding allocations, with the outcome feeding into the 2019/20 local government finance settlement. The negative RSG currently included within the Council's funding allocation for 2019/20 amounts to £399,900. *If the Government were to reduce this by half say, as an outcome of the consultation process, the Council's budget position would be bettered by £200,000 for 2019/20 and 2020/21 and bettered by £250,000 from 2021/22 onwards.*

- 4.9 Rural Services Delivery Grant – In the final Finance Settlement, the 2018/19 funding has been increased from £65 million to £81 million. This has meant extra RSDG funding for 2018/19. The £408,055 has been built into the Council's business rates baseline for 2018/19 due to the Council's Pilot status.

Council Tax

- 4.10 South Hams District Council's share of the council tax bill in 2018/19 was **9%**, being £160.42 out of an average Band D council tax bill of £1,822. The total income from council tax in 2019/20 is predicted to be £6.34 million. A 1% increase in council tax generates an extra £61,000 for South Hams.

Council tax referendum limit of £5 or less than 3% for District Councils

- 4.11 The Finance Settlement (February 2018) stated that for District Councils, increases of less than 3% or up to and including £5 (whichever is higher), can be made without triggering a council tax referendum. This is for 2018/19 and is indicative only for 2019/20 (this is to reflect the level of inflation).
- 4.12 For South Hams, a £5 increase in council tax equates to a Band D council tax for 2019-20 of £165.42 and equates to a council tax increase of 3.1%. Therefore the highest amount that South Hams District Council can increase council tax before triggering a referendum is £5 for 2019-20. A council tax increase of the higher of £5 or 2.99% per annum has been modelled in Appendix B for 2019-20 and beyond for illustration purposes.
- 4.13 The Government has not yet announced what the council tax referendum criteria will be for 2019/20.

5 BUDGET PRESSURES, SAVINGS AND INCOME GENERATION

- 5.1 Financial modelling has been undertaken for the next five years to predict the Council's financial situation for the short and medium term.
- 5.2 ***Appendix A*** to the Medium Term Financial Position sets out the Budget Pressures forecast for the next five years and the additional savings and income forecast. ***These figures in Appendix A show the changes to the existing base budget.***

(As set out in Appendix A)	2019/20 £	2020/21 £	2021/22 £	2022/23 £	2023/24 £
Cost Pressures	1,017,500	860,000	385,000	335,000	335,000
(Reduction)/ Increase in contribution to Earmarked Reserves	(458,916)	(60,000)	(13,000)	66,000	0
Savings and additional income identified	(217,250)	(256,250)	(106,250)	(77,250)	(1,250)

- 5.3 A description of the larger cost pressures is set out below.
- 5.4 **Salaries** – A 2% provision for a pay award has been included for 2019/20. This is explained in section 3.1.
- 5.5 **Devon Aligned service for Waste** – Members have previously agreed the principles of the Waste and Resource Strategy for Devon (aligned service) but with the exception of charging for garden waste. In order for the Council to move to the Devon aligned service, a cost pressure of £175,000 in 2020/21 and £175,000 in 2021/22 (totalling £350,000 p.a. from 2021/22 onwards) is estimated. The implementation date would be September 2020.

If the Council reneges on its commitment to move to the Devon aligned service, Devon County Council would likely consider other ways of recouping the additional expenditure that has been generated through higher disposal costs caused by the current South Hams service design (for example the mixed collection of food and garden waste in South Hams means that this material has to be hauled to Oxfordshire for composting, as opposed to the local composting facilities enjoyed by all other Devon Districts). Income from recycling credits may be compromised. In addition, South Hams is losing potential income from recycle sales because of the current sack collection method. This is now unsustainable due to demand from global recycling markets for 'clean' materials.

There would also be £125,000 of one-off implementation costs. These are indicative prices worked up by officers and are separate to the current procurement process. These prices are based on other Councils' experiences of moving to the Devon Aligned Service. It should be recognised that each Council starts from a different base which will affect the final figures.

This additional expenditure can be mitigated if, for example, the Council were to charge for garden waste collection and/or reduce residual household waste collection frequencies.

- 5.6 **Reduction in recycling income** – There is a recycle income pressure of £125,000 due to a fall in market prices.
- 5.7 **Blue and Clear recycling bag processing (safe working practice requirement at Torr Quarry)** – There is a cost pressure of £75,000 identified for this.
- 5.8 **Waste and Recycling Haulage contract** – A report was presented to the Executive on 14th June 2018 regarding the new contract. A cost pressure of £60,000 has been built into the financial modelling.

5.9 **ICT future service provision and support contracts** – It is anticipated that the ICT future service provision could cost an extra £150,000 annually from 2020/21 onwards and this has been reflected within the modelling in Appendices A and B. The contract for Civica is for five years (expiring end of March 2019) with an option to extend for a year. Officers will be presenting a report to Members in September 2018 with options for ICT future service provision. If the decision is for the Council to move away from the current model to a subscription based model, this would increase the annual revenue cost but there would be no future capital costs. However there would be implementation costs at the time of migration.

5.10 An extra £50,000 has also been included as a ICT cost pressure in 2019/20 onwards for support contracts, to better align the budget to actual expenditure. The ICT budget was set assuming that the Civica solutions introduced by the T18 Transformation Programme would perform as required. The cost pressure in 2019/20 is due to the continued use of additional software to replace elements of the Civica offer. In practice, additional solutions were procured in order to maintain services where using the Civica solution was not practical. Purchase of the following systems, which were previously unbudgeted for, was required:-

Northgate Land charges

Clear Core (enables single customer record)

IEG4 Revenues and Benefits to facilitate “My Account” for customers

Northgate Gazeteer – address database

IEG4 software – Automatic processing of changes of circumstances for revenues

The IEG4 software budget is funded by an increase in the housing benefit overpayment recoveries which has been built into the base budget as an income stream.

5.11 **Savings from re-procurement of contracts (leisure)** – the savings within Appendix A have been profiled to match the debt structure and repayment of the MRP (minimum revenue provision).

6. **OVERALL POSITION – BUDGET GAP**

6.1 Appendices A and B illustrates the overall financial forecast for the forthcoming five years. The Council’s Net Budget is £8.9 million in 2018/19. A Summary forecast is shown below of the potential budget situation if all of the budget pressures and the savings and income generation in Appendix A were approved. It also shows the situation if Council Tax is increased by the higher of 2.99% or £5 (shown in Appendix B) .

6.2 The following table illustrates the predicted budget gap from 2019/20 onwards for the Council as shown in Appendices A and B:

Cumulative Budget Gap	2019/20 £	2020/21 £	2021/22 £	2022/23 £	2023/24 £	Total Aggregated Budget Gap £
Modelling in Appendix B (assumes no reduction in -ve RSG and no Pilot)	994,998	1,348,174	1,387,697	1,374,691	1,360,553	6,466,113

6.3 In the modelling in Appendix B, the total budget gap is £994,998 in 2019/20 and this is predicted to rise to £1,348,174 in 2020/21. The aggregated Budget Gap is £6,466,113.

7 FINANCIAL SUSTAINABILITY AND TIMESCALES

7.1 The Council is progressing various options for closing the budget gap in 2019/20 and future years, to achieve long term financial sustainability. The table below sets out a timescale for those options and the various strands that the Council is exploring.

Option	Possible Budget Impact	Timescale
<p>Pensions Strategy The Council is obtaining specialist pensions advice on its Pensions position and progress on this will be reported to the October Audit Committee. The Council will look at options to reduce its revenue contribution for pensions, to aid affordability.</p>	Up to £200,000	Report to the Audit Committee October 2018
<p>Waste Procurement The Council is currently in a waste procurement process through competitive dialogue. The Council will consider a report in July 18 on the Detailed Bid stage of the competitive dialogue process. This is not included in the Modelling figures in Appendix B.</p>	To be quantified	Report to the Council meeting 26 th July 2018

Option	Possible Budget Impact	Timescale
<p>Council Tax Reduction Scheme The grant to Town and Parish Councils has been reduced by 9.85% over the four year period of the finance settlement. Members have an option over whether to withdraw funding in 2020/21.</p>	<p>£74,000 for 2020/21 onwards</p>	<p>Executive/Council September 2018.</p>
<p>Asset Review On 14 June 2018, the Executive considered a report on Council Owned Asset Investment and Development opportunities. The Council will prepare detailed business cases on the opportunities in the report and report back to Members.</p>	<p>To be quantified</p>	<p>Within three months</p>
<p>Commercial Property Strategy There is a separate report on the Executive agenda with regard to a Commercial Property Strategy.</p>	<p>To be quantified</p>	<p>Council 27th September</p>
Funding Options		
<p>Negative Revenue Support Grant The Government will publish a consultation on this although no timescale is yet known. If the outcome were to be that negative RSG is reduced by say 50%, the impact of this would be £200K in 19/20 and 20/21 and £250K in 21/22 onwards.</p> <p>The Government is seeking a fair and affordable solution to this issue however, as things stand, South Hams will pay the Government negative Revenue Support Grant from 2019/20, clawed back through the business rates system.</p>	<p>£200,000 in 2019/20 and 2020/21 and £250,000 in 2021/22 onwards</p>	<p>Anticipated to be known by December 2018 when the Draft Local Government Finance Settlement is published.</p>

Option	Possible Budget Impact	Timescale
<p>Business Rates Pilot status for 2019/20</p> <p>If the Devon Business Rates Pilot were to be successful for 2019/20, this could give further one-off extra business rates income in 19/20. Based on a 75% growth retention scheme, this could yield up to £250,000.</p>	<p>£250,000 in 2019/20 (one-year only)</p>	<p>December 2018 when the Draft Local Government Finance Settlement is published.</p>
<p>New Homes Bonus allocations for 2019/20</p> <p>The NHB allocation for 2019/20 is anticipated to be around £980,000, of which £500,000 is currently projected to be used to fund the Revenue Base Budget. The Council could chose to use a higher amount to fund the Revenue Base Budget but this would leave little funding available for the Capital Programme.</p>	<p>Up to £480,000</p>	<p>NHB allocations will be announced around December 2018. Decisions around its use will be made as part of the Budget Process.</p>
<p>Contributions to Earmarked Reserves</p> <p>The Council could decide not to contribute some of the amounts per annum into Earmarked Reserves. This will be considered in more detail as part of the September report to the Executive. Contributions to Earmarked Reserves are shown in Appendix C.</p>	<p>To be assessed</p>	<p>To be decided as part of the Budget Process</p>
<p>Use of Reserves as a temporary measure</p> <p>The Council has £1.85 million in Unearmarked Reserves. (The Council could temporarily utilise Reserves to balance an element of the 2019/20 budget, whilst longer term solutions are being implemented. This would be a very short term solution though.</p>	<p>To be assessed</p>	<p>To be decided as part of the Budget Process</p>

- 7.2 There is a Budget meeting being held with all of the Extended Leadership Team (ELT) in August to further identify ideas and options for closing the Budget Gap. These options will be presented to Members in future reports.
- 7.3 The diagram below shows the Government timetable of key dates. The key dates will be in May 2019 when more details will be known about the Funding Reform and Spending Review 2019. In November 2019, the baseline funding for business rates and the impact of transitional arrangements will be known.



8. NEW HOMES BONUS (NHB)

- 8.1 Appendix E sets out estimated amounts of NHB receivable in future years and possible uses of the NHB.

9. CAPITAL PROGRAMME 2019/20 AND PRUDENTIAL BORROWING

- 9.1 The Capital Programme is set by the Council annually and may be funded by sale proceeds from the disposal of assets (capital receipts), external grants and contributions, directly from revenue or from borrowing.
- 9.2 Capital Bids are being requested from Project Managers and a proposed Capital Programme for 2019/20 onwards will be presented to Members in a future report.

- 9.3 **Commercial Property Acquisition Strategy** – A separate report is on the Executive agenda for a Commercial Property acquisition strategy. Purchases made within the strategy will be capital expenditure and will be in addition to the projects outlined in the annual Capital Programme.
- 9.4 Prudential Borrowing - The Council will consider the use of prudential borrowing to support capital investment to deliver services and will ensure that the full costs of borrowing are taken into account when investment decisions are made.
- 9.5 The Council's published Treasury Management Strategy details its borrowing limits and specifies approved institutes for investment, (with maximum limits), based on credit ratings and other pertinent factors. The Council also publishes Prudential Indicators which set investment and borrowing performance indicators to ensure that the Council stays within these guidelines. The Council maintains regular engagement with our Treasury Management advisors, Link Services, and constantly seeks their advice on our strategic direction and key operational decisions.
- 9.6 Recommendations will be made in the September Medium Term Financial Strategy on the Borrowing Limits for 2019/20 onwards and the Council's Minimum Revenue Provision Policy Statement.

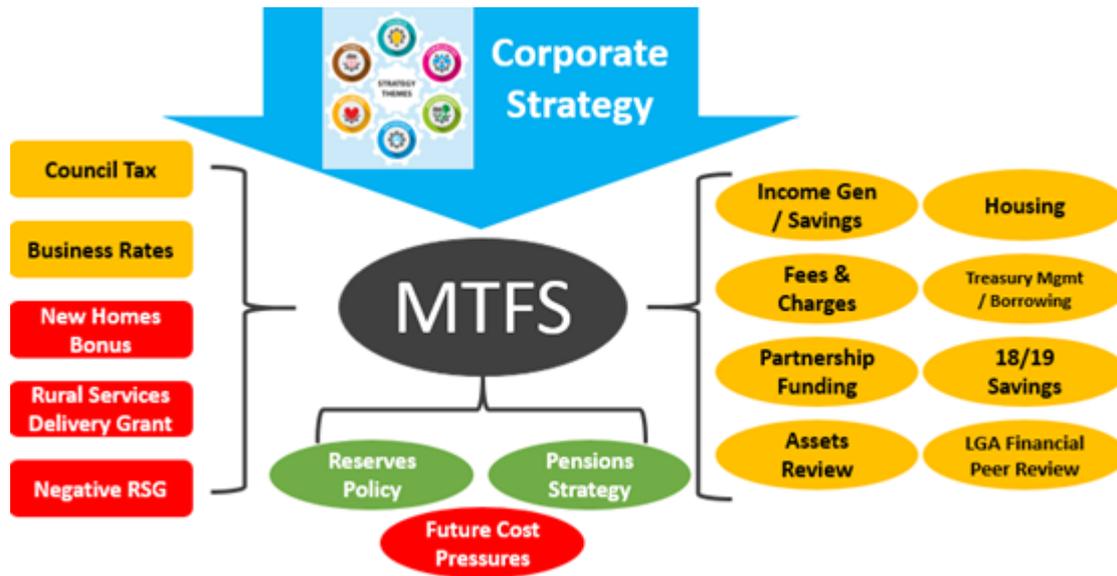
10. EARMARKED AND UNEARMARKED RESERVES

- 10.1 A schedule of the Council's Earmarked and Unearmarked Reserves is set out in Appendix D. The Council has just over £1.8 million in Unearmarked Revenue Reserves and £13 million in Earmarked Reserves (after incorporating the Council's share of the Business Rates Collection Fund surplus). The Council's Net Budget is £8.9 million in 2018/19.

11 NEXT STEPS

- 11.1 This report is a snapshot (a position statement) in July 18 and future Member decisions on the budget strategy will inform future figures within the Medium Term Financial Strategy (MTFS), which will be presented to Members at the Executive meeting on 13th September 2018. Officers held an informal workshop on the Medium Term Financial Strategy with Executive Members and relevant Chairs of Committees, where strategic principles for each element were discussed.
- 11.2 This is the starting point for developing a meaningful five year strategy that sets out the strategic intention for all of the different strands of funding available to the Council. The Council will then be able to rely on this to inform future decisions. The different elements that make up a Medium Term Financial Strategy are shown in the diagram below. In September 2018, Members will be asked to set the strategic intention for each of these components of the MTFS.

11.3 Make-up of the MTFS (Net Budget £8.9m)



11.4 Officers will continue to work with Members and the results of this will be incorporated into future Budget reports. Section 7 sets out the potential timescales against the areas identified.

12. IMPLICATIONS

Implications	Relevant to proposals Y/N	Details and proposed measures to address
Legal/Governance	Y	The preparation of the Budget annually is evidence that the Council has considered and taken into account all relevant information and proper advice when determining its financial arrangements in accordance with statutory requirements, and in particular, that it will set a lawful budget.
Financial	Y	The financial implications are summarised in Appendices A and B of the report. Appendix B shows that in 2019/20, the Council has a predicted £0.995m budget gap.
Risk	Y	Each of the budget options taken forward by Members will consider the risks of the option.

Comprehensive Impact Assessment Implications		
Equality and Diversity		Comprehensive Impact Assessments are completed for the budget proposals.
Safeguarding		None directly arising from this report.
Community Safety, Crime and Disorder		None directly arising from this report.
Health, Safety and Wellbeing		None directly arising from this report.
Other implications		None directly arising from this report.

Supporting Information

Appendices:

Appendix A – Budget pressures and savings

Appendix B – Summary of Budget position

Appendix C – Contributions to Reserves

Appendix D – Reserves (Earmarked and Unearmarked)

Appendix E – New Homes Bonus funding

Appendix F – Review of 2018/19 Budget Savings and Income Generation