

Report to: **Council**

Date: **27 September 2018**

Title: **Medium Term Financial Strategy for 2019/20 to 2023/24**

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**

Author: **Lisa Buckle** Role: **Strategic Finance Lead (S151 Officer)**

Contact: **Tel. 01803 861413**
Email: lisa.buckle@swdevon.gov.uk

RECOMMENDATION

It is RECOMMENDED that the Council:

- i) Notes the forecast budget gap for 2019/20 of £0.638 million and the position for future years;**
- ii) Notes the current options identified and timescales for closing the budget gap in 2019/20 and future years, to achieve long term financial sustainability;**
- iii) Approves Recommendations 1 to 10 as set out within the body of this report.**

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. Between 2009/10 and 2019/20, the Council's Core Government funding has reduced by £4 million.

- 1.3 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.
- 1.4 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.
- 1.5 **South Hams District Council is currently forecasting a £0.638m budget gap in 2019/20.** This is lower than the £0.995m budget gap for 2019/20 predicted in July 2018, due to the Government announcing in a technical consultation that its preference is to eliminate negative Revenue Support Grant (RSG) for 2019/20. The MTFs (September 18) assumes that negative RSG will be reduced to zero in 2019/20 - which improves the Council's budget position by £0.4m for 2019/20. This betterment has already been factored into the September modelling in arriving at the forecast budget gap of £0.638m for 2019/20. It is assumed that negative RSG remains in some form (e.g. as part of the business rates baseline reset) from 2020/21 onwards.
- 1.6 In 2020/21 the Council is facing a further budget gap of £0.865m (on top of the £0.638m in 2019/20). Therefore the budget gap over the next two years is in the region of £1.5 million.
- 1.7 It is important to note that this Medium Term Financial Strategy sets out the budget strategy for the Council for the next five years, with annual reviews and updates when items are further known or are announced by the Government (e.g. the Provisional Finance Settlement will be announced by the Government in December 2018).
- 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.
- 1.9 The Medium Term Financial Strategy (MTFS) was considered by the Overview and Scrutiny Panel on 6th September 2018. Minute O & S.33/18 refers. The Panel was of the view that any recommendations it made on External Borrowing levels would be pre-empting the views of the Audit Committee. As a result, the Panel did not feel it appropriate to make a recommendation on this part of the MTFS at this time. The Overview & Scrutiny Panel agreed with the other nine recommendations set out in the report.
- 1.10 The Audit Committee considered the Commercial Property Strategy on 6th September 2018. Minute A.17/18 refers. The view of the Audit Committee was that, subject to suitable governance arrangements

being in place, a total borrowing limit of £60 million (capped at £30 million before 30 April 2019) be agreed for the Commercial Property Strategy.

- 1.11 The Medium Term Financial Strategy (MTFS) was also considered by the Executive on 13 September. Minute E.30/18 refers. It was recommended to Council to approve recommendations 1 to 10 as set out in the presented report.

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.
- 2.2 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.
- 2.3 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.
- 2.4 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 Strategy 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 2.5% in July 2018.
- 3.3 The predicted interest rate forecast from our treasury management advisors, Link Services, is that interest rates will remain at 0.75% up to

September 2019. By December 2020 the bank base rate is predicted to increase to 1.5%.

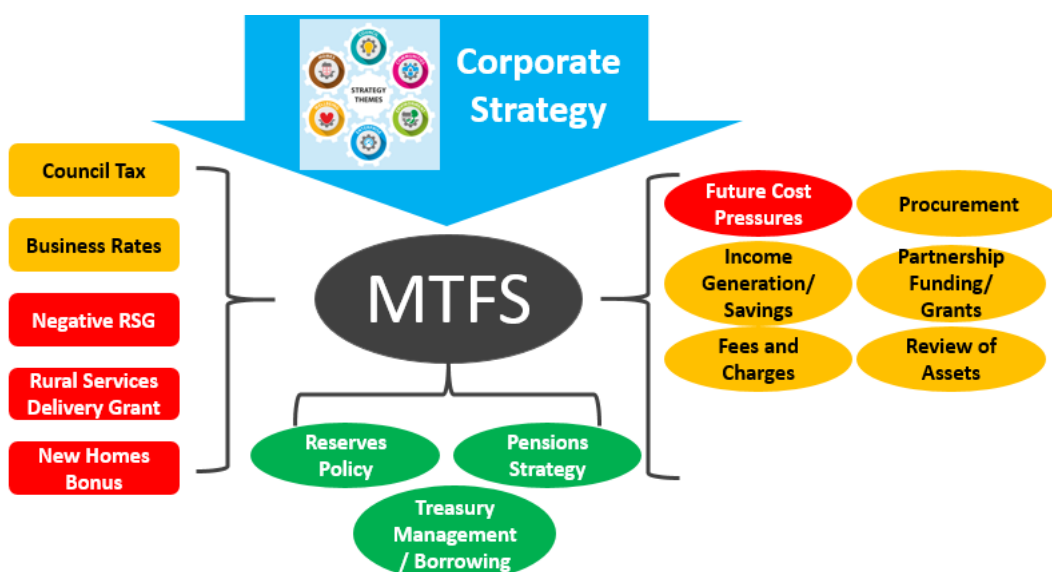
- 3.4 An increase in council tax of the higher of £5 or 2.99% for the next five years has been modelled for council tax purposes. This would equate to a Band D council tax for South Hams of £165.42 in 2019/20 as shown in Appendix B and equates to a council tax increase of 3.12%.
- 3.5 It has been assumed 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%.

4. THE COMPONENTS MAKING UP A MEDIUM TERM FINANCIAL STRATEGY (MTFS)

4.1 The Diagram below in 4.2 sets out all of the component parts which constitute the make-up of a Medium Term Financial Strategy. Appendix C goes through each of these components in detail and makes recommendations where appropriate. The recommendations are summarised below.

Items in Green denote those elements where the Council has a large degree of control over the setting of policies and strategies. Items in Amber denote those components of the MTFS where the Council has a degree of control. Red items signal components where the Council has hardly any control over funding allocations which are decided by the Government and future cost pressures which can largely be outside of the Council’s control or influence.

Net Budget £8.9 million 2018/2019



Council Tax

- 4.2 Recommendation 1: To set the strategic intention to raise council tax by the maximum allowed in any given year, without triggering a council tax referendum, to enable continued delivery of services. The actual council tax for any given year will be decided by Council in the preceding February.

Business Rates

- 4.3 The income from Business Rates which South Hams District Council retained in 2017-18 was the funding baseline of £1,800,829. The Council was not part of the Devon Pool in 2017-18 due to the risk of business rates appeals, but South Hams is part of the Business Rates Pilot in 2018-19.

Business Rates Pilot for 2019-20

- 4.4 Modelling which has been carried out on the application for 19/20 Pilot status shows that South Hams could gain approximately £250,000 of the £10 million projected 19/20 Devon Pilot gain. This is approximately half of the 18/19 predicted SHDC gain of £575,000. This additional funding of £250,000 would be a one-off amount for 2019/20 only.
- 4.5 Recommendation 2: To submit an application for Pilot status for 2019/20 and to agree a 40% District/34% Devon County Council/1% Fire split for the 75% scheme, with the agreement to remain part of the Devon Business Rates Pool for 2019/20 if the Pilot bid is not successful.

Recommendation 3: To actively lobby Central Government and Devon MPs to support a 2019/20 Devon Pilot bid

Recommendation 4: To actively lobby and engage with the Government, Devon MPs and other sector bodies such as the District Councils Network and the Rural Services Network, for a realistic business rates baseline to be set for the Council for 2020 onwards.

Negative Revenue Support Grant

- 4.6 The negative RSG currently included within the Council's funding allocation for 2019/20 amounts to £399,900. If the Government eliminates this, as an outcome of the consultation process, the Council's budget position is bettered by £400K for 2019/20 (this betterment has already been assumed in the modelling in Appendices A and B). The Council is hopeful the Government will reverse it, as this is the Government's preferred option in the consultation.
- 4.7 **The Medium Term Financial Strategy assumes that negative RSG will be reduced to zero in 2019/20** and this reduced funding pressure has been built into the latest modelling set out in this report. If the position changes, the MTFs will be updated to reflect this. It is

assumed that negative RSG remains in some form (e.g. as part of the business rates baseline reset) from 2020/21 onwards.

Recommendation 5: That SHDC responds to the technical consultation in support of the Government eliminating Negative Revenue Support Grant and continues to lobby for Rural Services Delivery Grant allocations which adequately reflect the cost of rural service provision.

New Homes Bonus

- 4.8 The Government released a consultation in July which stated their intention to increase the 0.4% baseline. They have also stated that 2019-20 represents the final year of NHB funding and from 2020 onwards they will explore how to incentivise housing growth most effectively and will consult on this issue.

Recommendation 6: To use £500,000 of New Homes Bonus funding for 2019-20 to fund the revenue base budget and then to reduce to £400,000 by 2020-21 and £250,000 by 2021-22 for modelling purposes.

Reserves Policy

- 4.9 Current Levels of Reserves: £1.849 million Unearmarked Reserves and Earmarked Reserves of £8.321 million (excluding the Business Rates Volatility Earmarked Reserve). The Council's Net Budget is £8.98 million for 2018/19. Therefore Unearmarked Reserves equate to 20% of the Council's Net Budget.

Recommendation 7: That the annual level of contributions to Earmarked Reserves (£722,300 as per Appendix E) and the adequacy of the existing level of Unearmarked Reserves (£1.8 million) and Earmarked Reserves (£8.3 million) is reviewed by Members as part of the budget setting process. This will assess the adequacy of Reserves levels, in light of future plans and pressures.

Pensions Strategy (Actuarial Valuation)

- 4.10 Recommendation 8 - That the Council takes specialist pension advice on the options for the Council's Pension position (informing the actuarial valuation), with the aim of reducing the current deficit contributions, increasing affordability, whilst best managing the pension deficit. It is also recommended that the Council has early dialogue with DCC and the actuaries with regards to the Council having an input into the actuarial assumptions used for the 2019 Actuarial Valuation. Options will be taken back to the Council's Audit Committee in January 19 to consider.

Treasury Management and Borrowing Strategy

- 4.11 The Council has taken external treasury management advice on the Council's overall borrowing levels and debt levels and this advice is attached in Exempt Appendix G. Their recommendation is that the Council limits its overall borrowing envelope for its whole operations and services to £75 million. This advice is based on a range of benchmarking of indices that they have undertaken. Borrowing needs to be proportionate and affordable and with always having regard to the risks involved in the repayment of the debt.

Recommendation 9 – That the Council sets an Upper Limit on External Borrowing (for all Council services) as part of the Medium Term Financial Strategy of £75 million as per Exempt Appendix G.

Future Cost Pressures

- 4.12 Recommendation 10 - To continue with the Local Government terms and conditions of employment Green Book for at least 2019/20. To review all options for reducing staff costs by varying terms from the Green Book from 2020/21, with an initial report back by the end of 2018/19.

Income Generation/Savings and Fees and Charges

- 4.13 The Council's Extended Leadership Team have been directed by the Executive to present further budget options to Members for income generation/savings/reduced expenditure, as part of the Budget Setting Workshop arranged for Thursday 11th October, taking into consideration the Council's corporate strategy.

Procurement

- 4.14 The Council is currently procuring its waste collection, recycling and cleansing services through a competitive dialogue process. The latest report was to Council on 26th July. Council Minute 25/18 refers. The procurement process will now continue to the 'Final Solutions' stage, with a further final report being brought to the Council meeting of 6th December 2018. Members will decide at this stage whether or not to award a contract. Any financial implications are not included in the Modelling in Appendices A and B.

Partnership Funding/Grants

- 4.15 The Community Task & Finish Group has proposed funding reductions of £32,316 to Partnerships (South Devon CVS and the South Devon AONB). This was considered by the Overview and Scrutiny Panel on 6th September 2018 and the Executive on 13th September and is recommended to Council as part of the budget process.

Review of Assets

- 4.16 The Council's Asset Base is £75 million at 31 March 2018. The Council will continually review and challenge its asset base in order to deliver the optimum value for money from the Council's Assets.

- 4.17 On 14th 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. Members will then be asked to attach an order of prioritisation for delivery to the business cases.

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 | 1,042,500 | 860,000 | 385,000 | 335,000 | 335,000 |
| (Reduction)/ Increase in contribution to Earmarked Reserves | (458,916) | 40,000 | 137,000 | 166,000 | 100,000 |
| Savings and additional income | (157,000) | (286,000) | (145,000) | (76,000) | - |

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 (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 -ve RSG in 2019/20 and no Pilot) | 638,348 | 1,503,674 | 1,654,447 | 1,742,691 | 1,829,803 | 7,368,963 |

- 6.3 In the modelling in Appendix B, the total budget gap is £638,348 in 2019/20 and this is predicted to rise to £1,503,674 in 2020/21 (the £1,503,674 assumes the budget gap in 19/20 of £638,348 has not been closed). The aggregated Budget Gap is £7.4 million over the five years.

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 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 in January 2019. |
| <p>Waste Procurement The Council is currently in a waste procurement process through competitive dialogue. The procurement process will now continue to the 'Final Solutions' stage, with a further final report being brought to the Council meeting of 6th December 2018. Any financial implications of this are not included in the Modelling in Appendices A and B.</p> | To be quantified | Report to the Council meeting 6 th December 2018 |
| <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> | £74,000 for 2020/21 onwards | Executive/Council February 2019. |
| <p>Asset Review On 14 June 2018, the Executive considered a report on Council</p> | To be quantified | As soon as the work on the |

| Option | Possible Budget Impact | Timescale |
|---|--|---|
| Owned Asset Investment and Development opportunities. The Council will prepare detailed business cases on the opportunities in the report and report back to Members. | | business cases is complete. |
| Commercial Property Strategy There is a separate report on the Council agenda with regard to a Commercial Property Strategy. | To be quantified | Council 27 th September |
| Savings identified by the Extended Leadership Team (ELT) The ELT held a Budget session on 15 th August. ELT were directed by the Executive to present further budget options to Members for Income Generation/savings/reduced expenditure, as part of the Budget Setting Workshop arranged for Thursday 11 th October, taking into consideration the Council's corporate strategy. | To be quantified | Members' Budget Workshop arranged for 11 th October |
| Funding Options | | |
| Negative Revenue Support Grant The Council is hopeful the Government will reverse Negative RSG in 2019/20, as this is the Government's preferred option in the consultation. The Medium Term Financial Strategy assumes that Negative RSG will be reduced to zero in 2019/20. It is also assumed that negative RSG remains in some form (e.g. as part of the business rates baseline reset) from 2020/21 onwards. | The Medium Term Financial Strategy assumes that negative RSG will be reduced to Nil in 19/20 | Anticipated to be known by December 2018 when the Draft Local Government Finance Settlement is published. |
| Business Rates Pilot status for 2019/20 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 | £250,000 in 2019/20 (one-year only) | December 2018 when the Draft Local Government Finance |

| Option | Possible Budget Impact | Timescale |
|--|------------------------|--|
| scheme, this could yield up to £250,000. | | Settlement is published. |
| <p>New Homes Bonus allocations for 2019/20</p> <p>The NHB allocation for 2019/20 is anticipated to be around £880,000, 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> | Up to £380,000 | NHB allocations will be announced around December 2018. Decisions around its use will be made as part of the Budget Process. It is highly likely the baseline will be increased from 0.4%. |
| <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 budget process.</p> <p>Contributions to Earmarked Reserves are shown in Appendix E.</p> | To be assessed | To be decided as part of the Budget Process |
| <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> | To be assessed | To be decided as part of the Budget Process |

- 7.2 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. CAPITAL PROGRAMME 2019/20 AND PRUDENTIAL BORROWING

- 8.1 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. 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.
- 8.2 **Commercial Property Acquisition Strategy** – A separate report is on the Council 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.
- 8.3 The Audit Committee considered the Commercial Property Strategy on 6th September 2018. Minute A.17/18 refers. The view of the Audit Committee was that, subject to suitable governance arrangements being in place, a total borrowing limit of £60 million (capped at £30 million before 30 April 2019) be agreed for the Commercial Property Strategy. This is based on the independent borrowing advice shown in Exempt Appendix G.
- 8.4 **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.
- 8.5 A Recommendation has been made as part of this report on the overall Borrowing Limit (£75 million) for the Medium Term Financial Strategy, with £60 million being for the Commercial Property Strategy and £15 million for other borrowing requirements.

9. Sensitivity Analysis and Risk Analysis

9.1 The Council carries out sensitivity analysis and risk analysis of its Budget Proposals and this is shown in Appendix F.

10 NEXT STEPS

10.1 This Medium Term Financial Strategy 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. This report is asking Members to set the strategic intention for each of these components of the MTFS.

10.2 Section 7 sets out the potential timescales against each of the areas identified.

11. IMPLICATIONS

| Implications | Relevant to proposals Y/N | Details and proposed measures to address |
|--|---------------------------|---|
| Legal/Governance | Y | <p>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.</p> <p>Appendix G to this report is considered exempt under paragraph 3 of schedule 12A of the Local Government Act 1972 in that it concerns the financial or business affairs of the Council. The public interest has been assessed and it is considered that, the public interest is better served by non-disclosure to the press and public.</p> |
| Financial | Y | <p>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 £0.638m budget gap.</p> |
| Risk | Y | <p>Each of the budget options taken forward by Members will consider the risks of the option.</p> |
| 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 –Modelling of the MTFS Position

Appendix C – Components of a MTFS

Appendix D – Schedule of Reserves (Earmarked and Unearmarked)

Appendix E – Contributions to Reserves

Appendix F – Sensitivity Analysis

EXEMPT Appendix G – Borrowing Advice from Treasury Management Advisers