MEDIUM TERM FINANCIAL STRATEGY

RESOURCES

Introduction:

1) The Council's financial plan forms part of the Council's Corporate Plan and will reflect the relative priorities set by the Council for the coming four years. Both are set within the emerging Community Strategy and LAA policy & performance framework.
2) Current grant & budget estimates identify a revenue budget gap in 2008/09 (circa £7.2m) and a smaller but significant gap in 2009/10 and onwards. This is in a context where the "predictable and stable" grant system is again subject to changes that could alter this council's grant by £ms. Current budget plans are based on a maximum estimated grant increase because this Council has been in a position where it has not received its full grant increase in the past 2 years and has been subject to a mechanism called "damping" that limits its increase. The Government is expected to lower the rate of increase of grant significantly because of national fiscal pressures and the Gershon agenda where it is forcing out budget savings by not funding Council cost pressures. The detail of this will be set out in the Comprehensive Spending Review (CSR07) expected to be published in October.

<u>Council Revenue Resource Envelope</u>

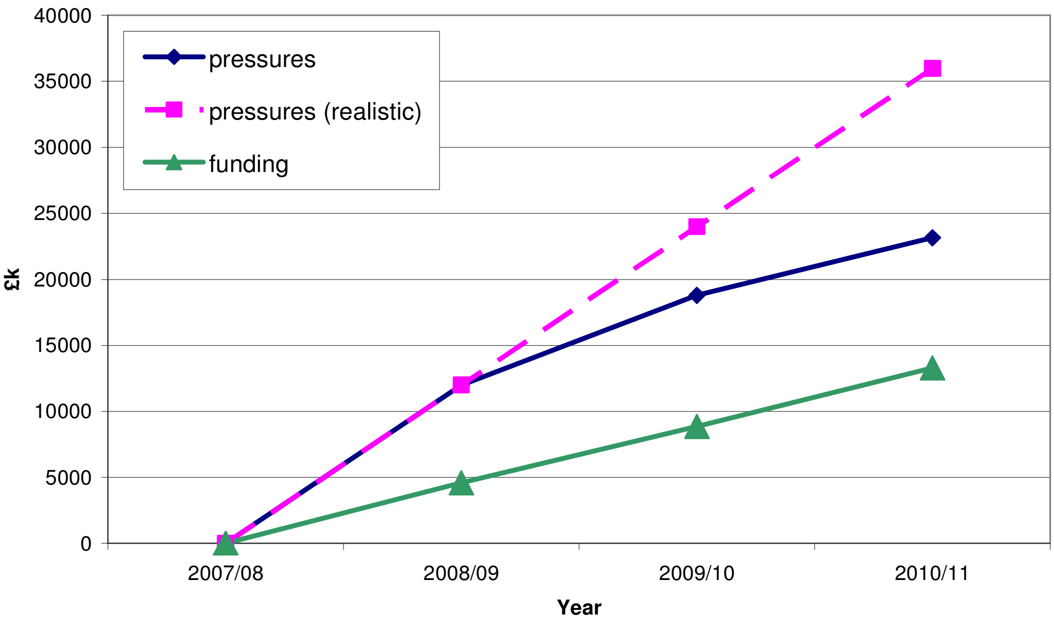
<u>Pressures for Growth</u>

3) Funding over the next few years will not match the pressures that are inherent in the plan. An analysis of these pressures and their causes (cost drivers) has been made for the next 3 years (see appendix 3). At present, these include the following items

- Pension increases
- Inflation
- Efficiency savings targets in 2007/08 that are not yet met
- Waste e.g. landfill tax, LATS
- Concessionary fares
- Adult care
- Learning Difficulties
- Car Parking
- Children's Placements
- Housing Benefit Admin grant reductions (effectively Department of Work & Pensions passing on their efficiency savings)
- Increased Leisure costs
- Changes to empty & void rate relief

– Home to School Transport
– Children's Services pensions & redundancy
– The Audit fees for the 2008/09 CPA inspection
– Planning
– People services costs
– Financing existing capital expenditure

Trend of budget funding versus budget pressures



4) This divergence of costs and funding is illustrated in the above graph. The outlook is that cost pressures will exceed funding by around £7m a year, unless cost pressures are contained (which is possible) or funding is increased (which is very unlikely). Because the council has a greater ability to identify and cost pressures one year in advance than 2-3 years in advance, the currently identified pressures for 2009/10 and 20010/11 may be an underestimate of the realistic position.

5) The challenge for the council is to manage pressures for growth in expenditure such that the rate of growth of expenditure is not greater than the rate of growth of income. Only when this is the case can the council's financial position be regarded as 'sustainable'.

6) This principle needs to apply to overall expenditure, and the major elements of expenditure. For example, in relation to the council's pay bill, if pay awards are expected to be c2-3% and in addition there are expected increases in pensions fund contributions of a further 1.3% per year together with incremental drift, it follows that the total cost is likely to be unsustainable without a reduction in FTEs through restructuring.

Outlook

National Picture

7) The figures included in the 2006 Budget indicate real terms growth of only 1.95% p.a. on Total Managed Expenditure over the three years of CSR07 (and 1.9% on current expenditure). Local government forms part of these figures.

8) The 2004 Spending Review provided for current education spending to increase by an annual average of 3.76% in real terms. Given the previous commitment to Education and current statements, it is likely that Education will see a significant real terms increase in current spending during the period of CSR07 also. This should translate into real terms growth in DSG budgets.

9) As part of the 2007 Comprehensive Spending Review, the treasury has included a far-reaching value for money programme to release the resources needed to address service pressures, involving further development of the efficiency areas developed in the Gershon review. This has already been flagged as an expectation of a 3% cash releasing efficiency target thoughout local government.

10) Local Government current spending has increased by 49.9% in real terms over the period since 1997/98, whilst total funding has increased by only 45.8%. The 'gap' has had to be met by increases in Council tax, which has risen in real terms in the period because of the gearing effect. When setting the 2007/08 budget the indicative increase for 2008/09 was required. This was at that time indicated as a 4.95% increase in Council Tax.

Grant review 2007 & Efficiency

11) Yet again a consultation has been issued on tinkering with some of the base data that calculates the local shares of Local Government funding which is then paid to each Council. This is done by means of a formula which calculates each Council's share of national resources. This is a complicated mechanism, but can be translated to a "Formula Spending Share" or FSS. The consultation is being assessed at present and the Cabinet Member for Resources will be making a formal response to this by 15th October. The following paragraphs outline highlights of what this contains.

12) We have assessed the changes that could occur from the grant review. The worst case figure from the exemplifications, which before grant damping is a loss of grant of £2.8m, if this change is used to update the grant based on the 2007/08 settlement for us with the damping %age unchanged nationally it would have equated to a loss of grant in 2007/08 of around £0.9m. The best case scenario will depend upon the damping arrangements – any gains above the level of the grant floor (the minimum

grant expectations) are always scaled back to fund those Councils who would otherwise be below the floor (i.e. would have received less than the minimum grant increase).

13) The consultation does not say how the 3% "Gershon" efficiency savings are going to be incorporated into the settlement, floors or damping however. The Council will need to incorporate a minimum requirement of 3% efficiency savings in all areas to reflect the government targets and falling grant.

14) The Concessionary Fares exemplifications have been excluded from these figures as this is extra money and the question here is more about whether we will be spending more than we get through the grant system – the assumption from the service is that grant funding is insufficient for existing costs and will be insufficient for future costs (the past record of funding versus costs is also included in Appendix 3). Exemplifications of the additional funding in 2008/09 for concessionary fares range from an additional £0.7m, £0.8m and £0.4m depending on the formula used. In April 2008 the Scheme is due to be rolled out nationally and the South West Local Government Association (SWLGA) are concerned that this may create problems with the funding allocation for Councils. They issued an extensive press release on 13th August 2007 concerning this issue. The SWLGA have now raised this issue with Government explaining the potential consequences of expanding this initiative, particularly as the South West is the fastest growing region in the UK, with high levels of tourist visitors who will be entitled to free bus travel.

15) There is also a potential for phasing out the grant damping – The Council gains under this (based on the 2007/08 settlement) as less money is clawed back with a lower floor - but this distorts the worst case position if included.

16) In addition it does not include exemplification for the proposed change to tax base to include student exemptions based on collecting data at different dates - this could be negative in grant terms for us because the Council adjusted its tax base for 2006/07 already to try and more accurately reflect student exemptions. If nationally more exemptions for students are included the tax base will fall at a national level and grant will be re-allocated to councils whose tax base falls more proportionally than others. This Council would then lose out.

Council Efficiency

17) On top of the savings requirement for 2008/09 onwards to match Government expectations (3% cashable savings each year), there is a further requirement to find savings to meet the funding gap anticipated through unfunded pressures (as set out in paragraph 3).

18) The Council has up to 2007/08 let services manage and finance their own pressures within service plans with guideline increases. The level of

savings found was significant in 2007/08 (£12m as set out in service plans including £1.2m on capital financing and £1m of corporate efficiency). The growth in budget for 2008/09 is currently estimated at £12m, with around £4.5m extra funding provisionally anticipated.

19) The SDG are currently repositioning the Efficiency Group to include an efficiency strategy. Following this, SDG intend that the Efficiency Group role will include :

- Monitoring (in terms of increased productivity and reduced costs)
  - Outcomes of the Service Transformation Programme
  - Service Plan outcomes
- Challenging and supporting the delivery as necessary and providing a high level summary to SDG
- Innovation
  - Identifying and leading cross service initiatives aimed at increasing productivity and reducing the cost base
  - Incubating new ideas and identifying and sharing best practice
- Scrutiny
- Monitoring VFM and investigating as necessary

20) SDG is also using the vehicle of the Efficiency Group to address the Council's budget resolution (2.8) that instructed them to work on ideas for reducing the overall cost base of the Council.

21) Services have been asked to follow up efficiency proposals within their areas as part of the service planning process. Examples of this include an income review, procurement, grants & sponsorship, shared services, the effects of PCT integration, and WorkSMART. In addition to this each area has been given specific areas of investigation e.g. parking in customer services, follow ups on base budget reviews. The Cabinet is asked to support that this list is within the considerations made by services in their planning for 2008/09 onwards.

<u>Council Tax</u>

22) An assumption has been made in the estimates to include a working assumption of a 3.95% increase in Council Tax for all of the three years. No guidance is yet available on what a "guideline increase" would be and without further guidance it is estimated that capping will be set at 5%, as it has been in previous years. A 1% variation in council tax amounts to £690,000

<u>Savings requirements in 2008/09 & beyond</u>

23) The gap will require that all services are required to look for sustainable efficiency savings for 2008/09 and onwards. Some imaginative, radical and innovative work will be required in services to meet such challenging targets, even in areas that have traditionally seen as "high priority".

24) In tandem with this, the perceived “pressures” could be critically examined and savings targets mitigated accordingly should some pressures be met in more cost effective ways. As a result of potential cost pressures, Gershon targets & limited funding the following guidelines have been developed for 2008/09 – 2010/11 service planning:

25) **Guideline 1**: In developing Service and Resource Plans, Services should be planning to absorb pressures. There needs to be clarity about impact of savings necessary to deliver financial balance so that O&S, Cabinet Members, SDG etc. can evaluate and consider re-allocation of resources to achieve financial balance, corporate priorities and manageable service.

26) **Guideline 2:** Services to plan for a minimum year on year 3% efficiency saving. This is in line with the national Gershon requirements. This also to be applied to all suppliers including those providing services via a contract, an SLA and the voluntary sector (where more than a minimal grant is given).

27) **Guideline 3:** All services to review income generating opportunities, particularly with a view to recovering the cost increases (which may be more than 3%) and looking at where full costs are not recovered at present.

28) **Guideline 4:** In order to meet the objectives set out in (25) above, many Service areas will need to be considering savings beyond the 3% level. Thus <u>all</u> services will need to consider efficiency savings in the range of 3% (minimum) to 6% (or more?) in service planning considerations.

<u>Income</u>

29) In addition to this all possible income sources must be required to increase income by at least an increase of 3%, whilst maintaining savings on gross expenditure. All services will also be asked to review their charging and costs levels to ensure that wherever possible full cost recovery is made for services that the Council provides that can be charged for, or if this is not to be the case, this should be the subject of an explicit funded decision to that effect.

<u>Reserves</u>

30) The Council reserves position was last reported in June (as part of the Outturn report). Target reserve level was £9m. Following a review of Strategic Director’s robustness of budget statements in June, taking into account the 2006/07 outturn position and 2007/08 emerging pressures, the target for the “day to day” level of reserves was increased to £10.2m with an optimal level of £11-£11.5m and minimum level of £6m. Forecast reserves are as follows, this assumes a balanced revenue position in 2007/08 with no overspends written off against reserves:

31) Contributions in later years will need to be reviewed in the light of updated risk assessments.

	2007/08 £'000	2008/09 £'000	2009/10 £'000	2010/11 £'000
Estimated Reserves @ 1st April each year	7,774	7,726	9,520	11,315
Contribution included in the Financial Plan	550	550	550	550
Additional contribution from service savings targets to restore reserves	664	664	664	
Senior Management Restructuring savings	73	73	73	73
Planned Contributions from adjustments in the Capital Programme (from 2006/07 Budget Report)	252	474	474	474
Proposed Transfer to Exceptional Risk Reserve	-1,400	-	-	
Loan to Bath Recreation Ground Trust (Council March 07)	-120			
UK Youth Games Funding (repaid in 2008/09 and 2009/10)	-67	33	34	
Estimated Reserves @ 31st March each year	7,726	9,520	11,315	12,412

Capital Resources

32) Current movement in capital financing from 2007/08 to 2008/09 with the existing programme is £925k above 2007/08 budget. This assumes full spend of the current capital budget. More slippage will reduce this growth so accurate forecasts later in the year are vital to good budget planning. The 2006/07 slippage that was not forecast at the end of 2006/07 has made a difference of between £0.5-£1m in the 2007/08 revenue budget.

33) For the existing indicative base programme (as set out in the February 2007 budget report) the movement in capital financing charges from 2008/09 to 2009/10 is around £0.5m and in 2009/10 to 2010/11 around

£1m. So overall over the next 3 years of the plan the indicative programme will add £2.5m to the revenue budget or a 2.5% increase in overall costs.

34) Current revenue budget pressures are such that to incur any unfunded additional capital expenditure will add further to the 2008/09 budget deficit. The capital strategy group has advised that an additional £2.5m in receipts is possible in 2007/08 & 2008/09, but no more. The budget resolution (February 2007) stated:

"…..and agrees that any further additions to the programme are subject to additional capital resources (government or third party funding and/or capital receipts) and an evaluation of the balance of benefits from additional capital investment and further reducing unsupported borrowing in the light of future years' revenue budget pressures."

35) Hence these receipts could be used to fund any additional essential capital expenditure in the 2008/09 budget, or they could be used to reduce debt charges and reduce revenue budget pressures.

36) In relation to Formula Spending Share (FSS) current capital financing charges (2007/08) are currently below the estimated FSS by around £2m. The existing programme's debt charges will close this gap to £1m in 2008/09, approximately £0.5m in 2009/10 and to £0.5m approximately above FSS in 2010/11. (These are approximate estimates as the increase in FSS in future years is unknown – in 2006/07 to 2007/08 it was only 3%).

37) Generally FSS reflects supported borrowing, so budget spend on top of this (i.e. unsupported borrowing) will cause the budget to exceed the FSS allocation.

38) In effect then, the existing approved programme will equalise capital financing spend and FSS. Any additions to this programme could then be funded within other service block allocations. This would then maintain the balance between government funding (as indicated by FSS) of supported borrowing and council capital financing budgets. Any new costs should then be met by services.

39) The Council's financing of any additional capital for 2008/09 and onwards should be seen in the context of additional funding supported by either;

- Additional capital receipts identified from corporate or service based assets (where they are thought sufficient enough not to repay or reduce unsupported borrowing).
- Unsupported borrowing financed by service savings or council tax increases within very limited parameters (as part of the cash allocations to services which could give services more autonomy over the balance of capital and revenue in their areas)
- Additional capital & borrowing funded by service savings (invest to save).
- Additional capital funded by grant.

Conclusions

40) Pressures to spend in 2008/09 and future years will be significantly greater than funding, and the gap between these 2 is likely to increase over time. A revenue budget gap of over £7m is forecast for 2008/09 and is likely to be at least as large in 2009/10 onwards.

41) To meet this gap services will need to plan for high levels of efficiency savings in the coming three years.

42) Services will be required to review charging levels to ensure full cost recovery. Major income generating services will be required to increase income by at least 3% (unless other targets have already been agreed by the Council).

43) Given existing revenue budget pressures, the Council cannot sustain any further unsupported borrowing to finance new capital projects in the medium term so only self funding or grant funded service proposals can be considered within service plans for 2008/09 at the very least.