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| **REPORT TO:** | **FINANCE & MANAGEMENT COMMITTEE** | **AGENDA ITEM:** 12 |
| **DATE OF MEETING:** | **21st JULY 2005** | **CATEGORY: RECOMMENDED** |
| **REPORT FROM:** | **DIRECTOR OF CORPORATE SERVICES** | **OPEN** |
| **MEMBERS' CONTACT POINT:** | **KEVIN STACKHOUSE (595811)** | **DOC:** u/ks/budget round 0607/july05 report |
| **SUBJECT:** | **FINANCIAL PLAN and UPDATED FINANCIAL PROJECTIONS to 2008/09** | **REF:** |
| **WARD (S) AFFECTED:** | **ALL** | **TERMS OF REFERENCE: FM08** |

## 1.0 Recommendations

1.1 That the revised financial projection on the General Fund to 2009 is approved.

1.2 That the revised financial projection on the Housing Revenue Account to 2015 is approved.

1.3 That the financial risks associated with the Council's financial plans and proposed actions are noted.

1.4 That the revised capital investment and financing programme to 2010 is approved.

1.5 That the budget and financial planning timetable for 2006/07 is approved.

## 2.0 Purpose of Report

2.1 The report reviews and updates the Council's financial plan and current medium-term financial forecasts. It considers both revenue spending and capital investment on the General and Housing Revenue Accounts.

2.2 It also sets out the proposed budget and financial planning timetable for the 2005/06.

2.3 The report effectively updates the Council's medium term financial position following the out-turn from 2004/05, together with setting the scene for the 2006/07 budget round.

## 3.0 Executive Summary

3.1 The Council's medium term financial forecast on its General Fund Revenue Account, continues to show a fairly sound position to March 2008. Projected general reserves show approximately £1.2m, above the minimum level required by the Council's financial strategy of around £1.075m.

3.2 However, the Council is likely to lose some fairly significant rental income from its General Fund during this planning period, as an industrial holding is likely to be sold. The cumulative effect of this would reduce general reserves to around £737,000 by March 2009.

3.3 The Council continues to face many financial risks and uncertainties and these are considered in detail. Given this, the Council should continue to plan its finances prudently and be in a position to address any adverse variances without jeopardising the longer-term financial position.

3.4 The longer-term financial projection on the HRA continues to improve, although it shows a projected cumulative deficit of around £404,000 by 2015. Again, there are risks and uncertainties that will affect the HRA and the position will continue to be monitored.

3.5 The Council's capital investment programme has been updated to 2010. This shows a shortfall in financing projected expenditure of around £1/2m. This is due to a slowdown in council house sales that is reducing the level of resources for future investment.

3.6 Due to the uncertainty involved, the financing programme does not include any further Government support in the form of general capital grants or borrowing allocations beyond 2005/06. Neither does it include any borrowing or asset sales apart from council houses.

3.7 Clearly, any additional resources stemming from these sources will help reduce the pressure on financing planned investment.

## 4.0 Detail

### FINANCIAL STRATEGY

4.1 The key components of the Council's financial strategy are set out below.

- To plan financially over 3 years for revenue and 5 years for capital investment.
- To maintain and keep under review an associated 3-year rolling financial projection on the General Fund.
- To maintain and keep under review a 5-year capital investment and financing programme.
- To maintain and keep under review a 10-year rolling financial projection on the Housing Revenue Account.

- To maintain a minimum general reserve as a contingency measure, of 10% of net revenue expenditure on the General Fund at the end of every 3-year planning period.

- To continually maintain and develop sound financial management through regular financial and budget monitoring.

- To assess the affordability of new spending proposals over the 3-year planning period (5-year for capital investment).

- To evaluate these proposals against the Council's approved scoring system.

- To review council spending in the light of changing priorities and new spending pressures.

4.2 The main cornerstones of the above strategy are medium term financial planning and in the case of the General Fund, reserve balances at a set **minimum** level at the end of every rolling 3-year projection.

4.3 This helps the council to focus on the resources that it will have available at the end of a 3-year planning period. More importantly it helps to identify where its resources are falling over this period and take action at an early stage to prevent any loss of financial stability.

## GENERAL FUND – MEDIUM TERM FINANCIAL PROJECTION

4.4 The latest approved financial forecast (February 2005) is summarised in the table below.

| **General Fund Projection to 31/03/2008 (as at Feb 2005)** | Probable Out-turn 2004/05 £ | Base Budget 2005/06 £ | Projection 2006/07 £ | Projection 2007/08 £ |
|---|---|---|---|---|
| • Net Revenue Expenditure | 8,884,380 | 10,132,690 | 10,516,380 | 10,642,160 |
| • Less Financing | 9,088,080 | 9,432,800 | 9,747,250 | 10,281,780 |
| **Surplus (-) Deficit for the Year** | **-203,700** | **699,890** | **769,130** | **360,380** |
| **General Reserves** | | | | |
| • Balance as at 1st April | 2,627,900 | 2,831,600 | 2,131,710 | 1,362,580 |
| • Less Surplus/Deficit | +203,700 | -699,800 | -769,130 | -360,380 |
| **BALANCE as at 31st MARCH** | **2,831,600** | **2,131,710** | **1,362,580** | **1,002,200** |

4.5 Following the 2005/06 budget round, the level of reserves pointed to a relatively sound financial position. However, it was noted that there were still underlying budget pressures within Council budgets and that demands being placed on spending were increasing.

4.6 The Council's strategy is to achieve a **minimum** level of general reserves of 10% of net revenue expenditure by 2007/08. Based on the projected net spending in the above table for 2007/08, this would equate to around **£1,065,000**.

4.7 The projected balance in the above table of just over £1m showed under this level. Therefore, the Council approved that this level be attained at the earliest opportunity.

4.8 In addition, the projections had assumed a contribution from the "Commutation Reserve" of £180,000 to help maintain the general reserve balance of at least £1m. Again, the Council has made a commitment to transfer this amount back at the earliest opportunity.

4.9 The main issue for the Council during the 2005/06 budget round, was identifying sufficient resources to meet new demands and aspirations for service improvements, without compromising the overall financial position of the General Fund.

**Updated Projection**

4.10 This projection has now been updated and revised to take account of in particular, the 2004/05 final out-turn. As the 2006/07 budget round is now effectively starting, it also extends to 2008/09, which is effectively now the revised financial planning period.

**Basis of the Financial Forecast**

4.11 This preliminary forecast takes into account inflationary projections and a number of known variations based on information currently available. This figures produced will be changed when actual information becomes available.

4.12 The primary focus of the forecast is to project the Council's future financial position. It will also form the basis for building the detailed budget plans for 2006/07 and beyond.

4.13 The following factors are included in the analysis:

- The base budget assumes the continuation of current service provision
- The effects of annual pay awards, increments and pension increases
- Inflation
- Annual increase in overall fees and charges
- Annual increases in the level of council tax
- Increase in the level of Government support
- Revenue implications of capital investment

4.14 These are considered in more detail later in the report.

4.15 The projection is detailed in **Appendix 1**, and is summarised in the following table.

| Revised General Fund Projection to 31/03/2009 | Base Budget 2005/06 £ | Projection 2006/07 £ | Projection 2007/08 £ | Projection 2008/09 £ |
|---|---|---|---|---|
| • Net Revenue Expenditure | 10,076,780 | 10,516,090 | 10,758,290 | 10,958,960 |
| • Less Financing | 9,432,800 | 9,799,430 | 10,318,060 | 10,522,650 |
| **Deficit for the Year** | **643,980** | **716,660** | **440,230** | **436,310** |
| **General Reserves** | | | | |
| • Balance as at 1st April | 2,974,660 | 2,330,680 | 1,614,020 | 1,173,790 |
| • Less Deficit (as above) | 643,980 | 716,660 | 440,230 | 436,310 |
| **BALANCE as at 31st MARCH** | **2,330,680** | **1,614,020** | **1,173,790** | **737,480** |

4.16 Projected reserves are forecasted to fall by 31st March 2009, to around £733,000. In the short-term, the favourable effect of the 2004/05 budget out-turn has increased balances and maintains the level above the 10% minimum as at 31st March 2008.

4.17 Although there continues to be a forecasted year on year deficit, the gap between income and expenditure is closing over the period. However, clearly the projected level of balances as at March 2009, is substantially below that required by the Council's financial strategy, i.e. £1.095m.

**Projected Loss of Income**

4.18 The main reason for this is the projected loss of income from one of the Council's main industrial holdings. This is due to the current leaseholder having an option to purchase the site in November 2006. They have indicated to the Council that they wish to purchase.

4.19 Although this would generate a fairly significant capital receipt for the Council, it would reduce annual rental income by around £170,000 per year (around £412,000 over this planning period).

4.20 Without this issue, balances as at 31st March 2009, would be in the region of £1.145m, above the 10% minimum required of £1.095m.

**The Financial Strategy**

4.21 On of the main principles of medium-term financial planning is that it helps the Council to focus on the resources that it will have available at the end of a 3-year planning period. More importantly it helps to identify where its resources are falling over this period and take action at an early stage to prevent any loss of financial stability.

4.22 Clearly, any projection should be viewed with a certain degree of caution. Although every effort has been made to take into account known spending pressures, some are less predictable. There are a number of factors which will affect this projection:

- **New spending pressures** and priorities that the council may wish to focus on over the next few years – if the Council wishes to find money for these new priorities it may to a certain extent, only come by achieving savings elsewhere. Clearly, the Gershon efficiency agenda should contribute to this.

- **Inflation** – **net** costs are expected to rise **on average** by 2.35% per year.

- **Growth in Council Tax Base** – in line with the continuing growth of the District, it has been assumed that the number of properties subject to council tax will increase by 1.5% in 2006/07, reducing to 1% in 2008/09.

- Council Tax Increase – assumes an annual increase of 4.5%.

- **Government Grants** – at this stage it has been assumed that general formula grant will rise by 2.5% per year.

**Financial Risk Analysis**

4.23 In addition, there is a range of factors that will have an impact on the above projection and these are detailed in **Appendix 2**, alongside action being taken to address these financial risks. A summary is provided below.

- **Insurance Costs** – now becoming a much lower risk although the market can change quickly. Premiums subject to full re-tendering exercise in September 2005.

- **Legal Costs and the Local Plan** – earmarked reserves provided to meet possible commitments, although it is uncertain how sufficient they will be.

- **Pensions** – still a concern. Need to continue to provide for increases in financial projections.

- **Planning Finance** – increased fee income but reducing Planning Delivery Grant and additional costs being incurred. Proposal is not to include further fee income in the mainstream budget pending certainty over Local Plan and PDG allocations

- **Government Grant** – increasing, but uncertainty makes planning difficult.

- **Job Evaluation** – possible costs from 2007/08 – this needs to be monitored closely.

- **Programmed Funding** – may become an issue – a detailed assessment is required.

- **Partnership Funding** – important to ensure proper contracts/agreements in place.

4.24 The above risks need to be balanced against other factors, which could have a potentially positive impact on council finances.

4.25 In particular, the Council currently receives a general grant settlement around £400,000 less than the Government's own formula assessment. If this were addressed in anyway, it would result in a higher grant settlement for the Council.

**Gershon Efficiency Savings**

4.26 There is a requirement on all Councils to make efficiency savings of 2.5% per year with effect from 2005/06. These savings are expected to be re-invested in front line priority services. The Government have indicated that they expect the Council to make on-going savings of around £240,000 per year of which, at least 50% should be cashable.

4.27 To-date, the Council has achieved and submitted to the Government savings of £66,500, of which £44,500 are cashable. In addition, other cashable savings have also been identified and approved by the Committee, as follows:

- Restructuring the Accountancy Unit (£38,775 to 2008/09)
- Reshaping Commercial and Licensing Unit (£16,700 to 2007/08)

4.28 None of these savings have been built into the 3-year projection as it is currently assumed that they will be diverted and utilised to improve services elsewhere.

4.29 In addition, certain issues have been identified in the Council's Annual Efficiency Statement from where the Council expects to meet its target.

**HOUSING REVENUE ACCOUNT (HRA)**

4.30 The Council has approved to retain the housing stock following a formal review carried out last year (July 2004). In addition, it was also resolved to keep under review the financial projections of the HRA.

4.31 Following this decision, the Council has been working on its business plan for the Government office. The final version is due by August 2005 and as part of the Plan, the Council is being directed to demonstrate the viability of the HRA to at least 2015.

4.32 An updated projection was considered during the last budget round. This highlighted a projected deficit of approximately £2.5m by 2015, although the account was sustainable until 2009.

4.33 In order to improve this situation, the Council has approved the setting-aside of £1m of additional capital resources to fund planned maintenance works included in the HRA, thus reducing the forecasted deficit.

4.34 The overall projections have also been updated, to include the 2004/05 budget out-turn, together with a review of projected repairs spending over the forecasting period.

4.35 The latest projection is shown in **Appendix 3**. Due in particular to the additional capital resources of £1m, the overall cumulative deficit is now much lower by 2015 at approximately £404,000. Current projections show that the HRA could be sustainable until 2012/13

4.36 However, similar to the General Fund, any projection should be viewed with a certain degree of caution. Although every effort has been made to take into account known spending pressures, some are less predictable.

**Housing Subsidy and Rent Increases**

4.37 There are a number of factors that will affect this projection, and in particular, future arrangements for Housing Subsidy and rent increases. The situation is very uncertain and can change from year to year which can make planning more difficult.

4.38 Similar to the General Fund, the HRA is not receiving its target management and maintenance allowances on the Government's formula. However, under the complexities of the subsidy system, any real terms increase in this area, may be offset by the subsidy system clawing back additional rent income over the rent-restructuring period to 2012.

4.39 This is due to the fact that the Council's actual rent is above the Government's guideline and formula rent.

**Housing Repairs**

4.40 The projected spending has been examined to take account of the effects of previous and planned capital investment in the housing stock. In particular, projected spending on responsive repairs has been reduced over the planning period compared to the previous forecast.

4.41 The revised level of spending will need to be monitored and controlled, especially in the light of the additional spending (compared to Budget) in 2004/05.

**CAPITAL INVESTMENT and FINANCING**

4.42 The Council is guided under a Prudential Code to set a 5-year capital investment programme. Clearly, this has to be based on assumptions about likely resources to be available and potential commitments facing the Council over this period.

4.43 Besides the schemes carried forward from 2004/05, there have been no major changes to the existing programme to 2009/10. However, due to a slow down in the number of council house sales in 2004/05, the shortfall in overall resources to finance all provisional expenditure in future years has risen.

4.44 The full investment and financing plan is shown in **Appendix 4.**

4.45 However, the overall investment programme shows a projected shortfall in resources of around £577,000 over the 5-year plan. Additional resources may be generated within the planning period and this will need to be monitored.

4.46 It should be noted that the Plans do not include resources of around £1m from the sale of sheltered accommodation in April 2005. Currently, this is earmarked to help deliver improvements to sheltered accommodation.

**Future Resources**

4.47 Resources projected to be available do not include any general Government allocations beyond 2005/06. This will depend on how resources are allocated by the Regional Housing Board in accordance with the East Midlands Housing Strategy. This is still to be determined.

4.48 Apart from partnership funding and any specific government grants that may be available, the Council's resources are very much dependent upon generating capital receipts. This is a risk in that their level from year to year can fluctuate (as seen) and cannot be accurately predicted, in particular council house sales. In addition, these resources are finite and once used, there is no guarantee that they will be replenished in the future.

4.49 Furthermore, it should be noted that the Council is committed until 2011/12 to the repayment of covenant (or loan) financing at around £1/2m per year. This is effectively the "first call" on capital resources. Clearly, these need to be included in the 5-year programme.

4.50 Under the Prudential System for Capital Finance, the Council does have the option to borrow. However, it would need to demonstrate that the associated financing costs could be met and sustained on its revenue accounts.

4.51 If existing programmes are to be continued, the need to identify additional resources is an important issue. The Council is working up a **Disposal Strategy,** a key task over the coming financial year to help deliver additional resources.

**BUDGET and FINANCIAL PLANNING TIMETABLE 2005/06**

4.52 The proposed timetable is detailed in **Appendix 5.** This is line with previous years and follows legal practice in ultimately setting the council tax by March 2006 and production of the Annual Statement of Accounts by 30th June 2006.

4.53 Further items have also been included in respect of:

- Budget consultation
- Training seminars
- Provision of monitoring information
- Tender for the provision of Insurance