REPORT TO:	**FINANCE AND MANAGEMENT COMMITTEE**	**AGENDA ITEM: 10**
DATE OF MEETING:	**15th FEBRUARY 2011**	**CATEGORY: RECOMMENDED**
REPORT FROM:	**DIRECTOR OF CORPORATE SERVICES**	**OPEN**
MEMBERS' CONTACT POINT:	**KEVIN STACKHOUSE (595811)** **kevin.stackhouse@south-derbys.gov.uk**	**DOC:** u/ks/budget round 201112/final budget proposals 1112
SUBJECT:	**FINAL BUDGET PROPOSALS 2011/12 and FINANCIAL PLAN to 2016**	**REF:**
WARD(S) AFFECTED:	**ALL**	**TERMS OF REFERENCE: FM 08**

1.0 Recommendations

1.1 That estimated net General Fund Revenue Expenditure totalling £12,370,916 for 2010/11 and £11,878,784 for 2011/12 is recommended to Council on 28th February 2011.

1.2 That a Council Tax level and Band D equivalent rate for 2011/12 is recommended to Council on 28th February 2011.

1.3 That the Medium-term Financial Plan to 2016 on the Council's General Fund Revenue Account as detailed in **Appendix 1** is approved.

1.4 That the financial projection on the Housing Revenue Account to 2021 as detailed in **Appendix 2** is approved.

1.5 That the 5-year capital investment and financing plan to 2016 as detailed in **Appendix 3** is approved.

1.6 That on-going cashable efficiency/budget savings (in addition to those identified in this report) of **£280,000 per year** are identified by March 2012 with progress being reported to the Committee on a regular basis during the coming year.

1.7 That the Council continues to roll out its procurement and transformation programme in order to generate resources beyond 2012/13.

1.8 That the outcomes of the current review of the HRA Business Plan and Self-Financing proposals are reported to the Committee in June 2011.

1.9 That the report of the Council's Section 151 (Chief Finance) Officer under Section 25 of the Local Government Act 2003 is noted.

2.0 Purpose of Report

2.1 To detail the Council's final budget proposals for 2011/12 and medium term financial projections on its main revenue and capital accounts. This includes an assessment of the overall budget and level of reserves as required by the Local Government Act 2003.

2.2 The proposals will form the basis of setting the Council Tax for 2011/12 by Council on 28th February 2011.

The Council's overall proposed base budget for 2011/12 and projected medium-term financial position was reported in detail to the Committee on 13th January 2011 (details are available at: http://cmis.south-derbys.gov.uk/CmisWebPublic/Meeting.aspx?meetingID=1420

2.3 This report does not repeat those details but firms up the position following a period of scrutiny and consultation. In addition, it reflects, in particular, the financial implications of service reviews approved by the Committee in December 2010 and January 2011, together with the results of the 2010 Actuarial Valuation of the County Council Pension Fund.

2.4 Furthermore, changes to the final financial settlement approved by central government are also detailed.

2.5 The report also provides an overview of the Housing Revenue Account and the 10-year financial projection that was considered by the Housing and Community Services Committee on 3rd February 2011.

2.6 The report is divided into the following sections.

- Section 3: General Fund Revenue Account
- Section 4: Housing Revenue
- Section 5: Capital Investment
- Section 6: Council Tax
- Section 7: Report of the Chief Finance Officer under Section 25 of the Local Government Act 2003

3.0 General Fund Revenue Account

3.1 The report in January highlighted projected budget deficits over the life of the Medium Term Financial Plan to 2015/16. These are shown in Table 1.

Table 1:
Projected Budget Deficit / Surplus (-)

YEAR	£
2010/11	-175,263
2011/12	887,152
2012/13	525,328
2013/14	696,372
2014/15	750,955
2015/16	1,016,524

3.2 Based on the associated spending plans and after allowing for certain cost pressures in the future, the projected level of general reserves were those as shown in Table 2.

Table 2:
Projected General Fund Reserves

YEAR	£
2010/11	3,425,813
2011/12	2,143,661
2012/13	1,333,333
2013/14	326,961
2014/15	-673,994
2015/16	-1,960,518

3.3 As Tables 1 and 2 shows, the projected deficit cannot be sustained beyond 2012/13 without identifying further budget savings.

Budget Savings and Other Changes since January

3.4 As previously reported to the Committee in December 2010 and January 2011, the following proposals have been approved and confirmed following consultation and contractual negotiations. The budget savings over the next 5 years are summarised in Table 3, below.

Table 3: Budget Savings Confirmed

Review of Senior Management and Restructure of the Community Services Directorate	£1,749,923
Retendering of Leisure Management (Etwall and Green Bank Leisure Centres)	£763,464
Total Budget Savings	**£2,513,387**

3.5 In addition, other changes have been made to base budget figures for 2011/12 and projected figures to 2015/16. These are summarised in Table 4.

Table 4: Other Changes to Base Budget Figures (over 5 years)

Increase in contributions to the Pension Fund following Actuarial Valuation (see below)	£147,054
Further savings made in Grounds Maintenance pre tendering process	- £110,188
Reduction in government grant between the provisional and final settlement	- £10,766
Transfer of Foston Travellers Site to the County Council – residual costs in 2010/11	£5,096
Adjustment to reflect the actual Tax Base approved in January	£1,071
Total Changes (increase in overall expenditure)	**£53,799**

2010 Actuarial Valuation of the Pension Fund

3.6 The MTFP had allowed for an increase in pension contributions of 1.5% per year on pensionable pay from 2011/12. The actuarial valuation of the Pension Fund was confirmed by the County Council on 31st January. This has set the Council's contribution rates for the 3 years 2011/12 to 2013/14.

3.7 The Council's current contribution rate is 19.9%, made up of 12.6% current service contribution, plus 7.3% for past service deficits. The later amount is designed to meet the projected deficit over time on the Pension Fund that has been building up in recent years.

3.8 This deficit has been increasing due to the liabilities on the Fund in the form of payments to pensioners, increasing at a greater rate than assets in the form of investment income.

3.9 The Council's rate for the following 3 years has been confirmed as follows:

- 2011/12 – 22.1%
- 2012/13 – 22.5%
- 2013/14 – 22.7%

3.10 Therefore, the overall rate will increase by 2.8 % over the next 3 years from 19.9% to 22.7%. Within this, the current service rate has actually decreased from 12.6% to 11.8%; it is considered that this reflects a "younger" workforce on average compared to the last valuation of 3 years ago.

3.11 However, the rate for the past service deficit has increased more significantly from 7.3% to 10.5% in 2011/12, with further increases to 11% in 2012/13 and 11.1 % in 2013/14. This appears to follow a general trend as liabilities continue to increase greater than assets.

3.12 Commentators believe that overall reductions in the workforce across local government, together with pay freezes, are having an adverse impact compared to previous years. This is because there is a lower base on which to recover the past deficit.

Effect on the MTFP

3.13 In cash terms, the MTFP had allowed for an increase of approximately £60,000 per year from 2011/12. This included the past service deficit of those staff transferred as part of the Corporate Services Partnering arrangement.

3.14 The actual increase is estimated at £90,000 per year and therefore a further £30,000 per year has now been included in the MTFP.

Other Changes

3.15 The increase in pensions has largely been offset by further budget savings identified in the Grounds Maintenance Service.

The Financial Settlement

3.16 The Government's proposals were reported in detail to the Committee on 13th January. The provisional figures released in December 2010 were broadly confirmed on 31st January when the final settlement for 2011/12 and the indicative settlement for 2012/13 were laid before Parliament.

3.17 Some minor errors and inconsistencies were corrected but the main change was that £**9m** nationally was added to Formula Grant for 2011/12 only. This was to mitigate some of the impact on shire districts of transferring responsibility for concessionary fares to upper tier authorities.

3.18 However, this appears to have been paid for by reducing overall Formula Grant in 2012/13 by £**10m**. The effect on South Derbyshire is that although Formula Grant has increased by approximately £42,000 (0.7%) in 2011/12, it has been reduced by £52,000 (1.0%) in 2012/13 – an overall loss of £10,000 compared to the provisional settlement.

3.19 Future year's estimated grant has been left at that projected in January and is based on an overall reduction in Formula Grant of 28% over the 4 years to 2014/15.

3.20 The combined effect of the changes highlighted in Tables 3 and 4 on the projected budget deficit and level of general reserves is shown in Tables 5 and 6 below.

Table 5:
Projected Budget Deficit
(Revised)

YEAR	£
2010/11	118,914
2011/12	434,771
2012/13	19,253
2013/14	117,610
2014/15	146,257
2015/16	404,675

Table 6:
Projected General Fund Reserves
(Revised)

YEAR	£
2010/11	3,131,636
2011/12	2,301,865
2012/13	1,997,612
2013/14	1,570,002
2014/15	1,173,745
2015/16	499,070

3.21 The updated projection is shown in **Appendix 1**. The overall effect of the budget savings and other changes is clearly positive on the financial position.

3.22 However, the level of general reserves is still projected to be only £499,070 by 2015/16 – approximately 50% of the approved minimum level of £1m. This is because there is still an on-going budget deficit which currently will need to be met from reserves.

Capital Commitments

3.23 As reported in January, provision has been made within the MTFP (earmarked in general reserves) to meet capital commitments. Identifying resources to meet these would also improve the situation further.

3.24 As previously reported, certain property transactions are currently in the process of being completed, the proceeds of which would contribute quite significantly to the £1.5m required over the next 5-years, with a consequential increase in the level of reserves shown in Table 6.

3.25 Although these transactions are progressing well, the receipts are still not certain, being subject to full planning approval and contractual negotiations. However, if completed as planned, receipts could be generated by March 2012 which would cover the first of the capital commitments in 2011/12 and 2012/13.

On-going Budget Deficit

3.26 However, as shown in Table 4 there is still an underlying budget deficit over the planning period. Excluding the one-off costs of a District Election in 2015/16 (of £125,000) the budget deficit by this year would still be approximately £280,000 based on current spending plans.

3.27 In addition, there will be a requirement for further capital commitments (estimated at £250,000) beyond 2015/16 for vehicle replacements.

Future Budget Savings – Indicative Target

3.28 Therefore, based on these projections further budget savings will be required well before 2015/16. These will be required in order to reduce the build-up of future deficits and to protect reserves above £1m.

3.29 From 2012/13, it is estimated that on-going savings of at least **£280,000** per year are required to deliver this strategy.

Provisions and Risks

3.30 As reported in January, the MTFP does not include any new resources (revenue or capital) for additional investment or service development. Provision continues to be made for items such as the interim costs of the pay and grading review, together with provisions for growth of the District and inflation.

3.31 However, the national grant position beyond 2012/13 remains uncertain. As reported in January, the Council is set to benefit from the New Homes Bonus and this could help the overall financial position. However, its funding also remains uncertain beyond 2012/13.

Proposed Actions

3.32 Some further project work already in place should generate resources to help improve and maintain the Council's finances on a sound and stable footing. However, detailed budget savings together with the timing of implementation are at this stage, by no means guaranteed.

3.33 Draft proposals with supported business cases will be reported to Committee during the year. In summary this will include:

- Tendering of the Grounds Maintenance Service (already approved and at Invitation to Tender Stage)

- Review of procurement and transformation in retained services, supported by the Council's Strategic Partner for Corporate Services

- On-going efficiency programme through targeted service and functional reviews; the planned reviews are being managed initially through the Council's Buisness Improvement Group.

Further Review

3.34 It is considered that the Council will need to continue to review its budgets to ensure that the financial position is sustained and to ensure that it is in a position to release resources to meet the on-going budget deficit and for service investment. At the very least, spending pressures may well arise from the Government's new Localism Bill, for which detailed proposals are awaited.

4.0 Housing Revenue Account (HRA)

4.1 This was considered in detail by the Housing and Community Services Committee on 3rd February. Following the review of the HRA's base budget, the Government's subsidy settlement for 2011/12, together with a proposed rent increase for 2011/12, the 10-year financial projection was updated. This is detailed in **Appendix 2**.

4.2 This shows a worsening position compared to the previous projection that was approved in October 2010. The revised projection shows that the HRA will continue to operate in deficit. The first year that the HRA falls below the £1/2m minimum reserve required by the Financial Strategy is 2014 compared to 2017 previously.

Rents and Housing Subsidy

4.3 This worsening position is mainly due to the proposed average rent increase of 5.4% being less than the national guideline of 6.8% and consequently below the overall increase of 7.2% to achieve rent convergence by 2015/16. However, the associated payment to the national housing pool will be greater than estimated as the system assumes that the higher guideline rent increase of 6.8% is implemented.

4.4 The Council's negative subsidy payment to the national pool will increase by 19% from £3,363,479 in 2010/11 to £4,011,638 in 2011/12 (around 39% of rent income). This is approximately £185,000 greater than estimated in the previous projection, mainly due to a higher guideline rent increase and lower capital costs.

4.5 A lower average increase in rent clearly protects individual tenants from higher charges. However, the net effect in the overall HRA is a loss of income of approximately £175,000 per year.

4.6 Some of this loss will be mitigated through a new policy approved by the Housing and Community Services Committee of reletting properties becoming vacant at the full formula rent. In a full year, this is estimated to generate £44,000 in overall rental income.

4.7 In addition, full rent convergence will not occur until 2017/18 – 2 years later than the national guideline of 2015/16. This is based on the current housing finance system.

4.8 With a projected deficit and a faster reduction in reserves, this will mean that the HRA will be come unsustainable much sooner than previously estimated. In the absence of any other changes, this will require a continuing review of all income and expenditure.

HRA Business Plan

4.9 A review of the HRA Business Plan is currently being undertaken and it is planned to report recommendations in June 2011. The review will take account of:

- Tenant priorities
- The investment requirements of the stock
- The affordability of capital debt
- Service provision including staffing levels
- Potential new income streams

4.10 The review will take a 30-year view as well as a concentrated look at the requirements for the next 5 years. It will aim to project the business viably into the future.

Reform to the National System

4.11 Following the publication of the Comprehensive Spending Review (confirmed in the "Local decisions: a fairer future for social housing" consultation paper of 22nd November 2010) the Government confirmed that they were going to introduce a fundamental change to national housing finance.

4.12 This will be based on a self financing model where the Council will be able to manage its HRA resources outside of a national system. This would be in return for taking on a share of the national debt attributable to council housing.

4.13 The Government released their final implementation proposals on 1st February. This confirmed that the current subsidy system will end on 1st April 2012 to be replaced by a self-financing framework.

4.14 Whether the Council will be able to afford self-financing will need to be considered closely. It is expected that an analysis of the Council's position will be reported alongside the Business Plan Review in June 2011.

5.0 <u>Capital Investment</u>

5.1 The approved capital programme is shown in **Appendix 3**. The only change from that reported in January is that the Government has confirmed that its funding for Disabled Facility Grants in 2011/12 will be at least equivalent to 2010/11 for each council, i.e. £269,000 for South Derbyshire.

5.2 Due to the lack of its own resources, the Council is ever reliant on external financing and contributions for future capital investment.

5.3 The main scheme for redeveloping Swadlincote Town Centre is nearing completion and the provision of community and recreational facilities continues to be made through Section 106 funding.

5.4 Although government funding for disabled facility grants and council house improvements is set to continue, other forms of capital funding are expected to be reduced over the next 4 years.

5.5 This will provide a challenge for the Council to deliver actions in its Asset Management Plan. This includes the current Depot redevelopment, together with iniatives around enabling land and assets to deliver affordable housing and economic development.

5.6 The Council's proposed Asset Management Plan (AMP) for 2011 to 2015 was considered at Item 8 on this Agenda.

5.7 Similar to revenue, the capital programme does not allow for any new investment. Service pressure remains in areas such as the provision of Disabled Facility Grants and to invest in new recycling facilities. Therefore, generating capital resources through the AMP will be a key factor in helping to realise future investment.

6.0 <u>Council Tax</u>

6.1 The MTFP assumes for planning purposes that council tax increases by 2.5% each year, 2011/12 to 2015/16. As part of the financial settlement, the CLG have confirmed that will provide an incentive for local authorities to freeze their council tax increases for 2011/12.

Council Tax Freeze (Specific) Grant

6.2 Where an authority freezes the council tax for 2011/12, i.e. sets a nil increase, a specific grant will be paid to effectively reimburse the resources lost, to the equivalent of a 2.5% increase. This grant will then be paid for the next 4-years (2011/12 to 2014/15) to reflect that the loss of income is cumulative over future years. The grant will be worth around £480,000 over 4-years.

6.3 Therefore, the Council is in a position to consider and take advantage of this as the financial plan indicated a 2.5% increase in 2011/12. Setting a lower increase between 0% and 2.5% would not qualify for the grant - it has to be a freeze. The Council could in fact be worse off by setting a lower level (as shown in Table 20, below).

6.4 The CLG will effectively pay for a 2.5% increase for the next 4-years. It will be adjusted each year to reflect changes to the tax base so the Council is protected over this period and the effect is neutral over the MTFP for 4-years.

6.5 However, as the grant is only payable for 4-years, there will be a shortfall in the 5th year of the MTFP (2015/16). This shortfall is estimated at approximately £156,000 (Table 7, below).

6.6 This can be compared with setting a lower increase to ascertain where a lower level in 2011/12 could in fact be more beneficial over 5-years, compared to the shortfall of £156,000. This is summarised in Table 7.

Table 7: Comparison to the MTFP of Council Tax Freeze Versus Lower Tax Rises for 2011/12

Loss of Income from Freeze (5-years)	- £640,973
Replace with Specific Grant (4-years)	£484,575
Shortfall over 5-years	**- £156,398**
Loss of Income - Over 5 Years	
1% Increase	-384,821
1.5% Increase	-256,547
1.75% Increase	-192,410
2% Increase	-128,274

6.7 The table shows that with a 1% increase, the loss of resources over 5-years (compared to the planned 2.5%) is higher at £384,821 than the loss of a freeze at £156,398. This is the case at up to 2%, where the loss is then lower than the freeze at £128,274.

6.8 If a council tax freeze is implemented for 2011/12 the Band D rate will remain at the level set for 2010/11, i.e. **£150.25**

6.9 In a Government Statement of the 13th December 2010, the Secretary of State said:

"The Government also want to ensure that council tax payers are protected against Authorities that reject the offer and impose excessive council tax rises. We will introduce powers for residents to veto excessive council tax increases through a local referendum. In the meantime, the Government will take capping action against councils that propose excessive rises.

When the House debates the final local government finance report next year, I will set out the capping principles. I will also publish shortly details of the figures that will be used to compare authorities' budgets between years, should capping be necessary. The previous Government had planned to cap the police authorities of Greater Manchester and Nottinghamshire after they set excessive increases in 2010-11. Subject to challenge, we will ensure that, should they decide not to freeze the council tax, neither can impose an increase of over 2.5% in 2011-12."

6.10 Given this, it is considered by many commentators that this is a signal the Government would like the capping limit to be very close to 2.5%.

6.11 The General Fund projection in **Appendix 1** assumes that the Government's offer is accepted and the effects as shown in Table 6 have been built into financial projections, at this stage.

6.12 This is ultimately a decision for the Council which will be considered and determined at its meeting on 28th February 2011 in accordance with statute. The Committee is required to make a recommendation to Council on the level of council tax.

7.0 Section 25 Report (under the Local Government Act 2003)

7.1 The Council's Section 151 (Chief Finance) Officer is required to provide an overall opinion on the robustness of the estimates included in budgets and the adequacy of Council reserves. The commentary is set out in the sections that follow.

Comments of the Chief Finance Officer

7.2 This report and that considered on 13th January 2011, highlights the risks and uncertainties surrounding the Council's financial plans and proposed actions it intends to take over the medium term to maintain a sound financial position.

7.3 It is considered that estimates of expenditure are prudent in that they provide for inflation and other known variations, based on the most up-to-date forecasts and available information.

7.4 In addition, a realistic but prudent view has been taken regarding projected income levels from fees, charges and short-term investments. This includes the likely effects of future central government funding in the form of Formula Grant and the New Homes Bonus.

7.5 The compilation of detailed budgets has been undertaken in conjunction with service managers. The Council has established performance and budget - monitoring arrangements in place to help ensure that Council finances are monitored effectively. This includes a quarterly report to this Committee.

7.6 The Council's Financial Strategy directs the Council to plan its spending over a 5-year rolling period. This provides an indication of the sustainability of spending plans and allows sufficient time in which remedial action can be implemented to address any issues.

7.7 Table 8 shows the projected level of revenue reserves over this planning period, i.e. 2011 to 2016.

Table 8: Projected Level of Revenue Reserves

FUND	MARCH 2011 £'000	MARCH 2012 £'000	MARCH 2013 £'000	MARCH 2014 £'000	MARCH 2015 £'000	MARCH 2016 £'000
General Fund Reserves	3,132	2,302	1,998	1,570	1,174	499
Housing Revenue Account	2,157	1,509	976	715	222	- 313
Other Earmarked Reserves	535	200	205	210	195	195

7.8 The Council, based on the recommendation of the Chief Finance Officer, has approved to set a <u>minimum</u> level of General Reserves of £1m on the General Fund and £1/2m on the Housing Revenue Account by 2016. This was after an assessment of the financial risks the Council faces and their potential impact upon the overall financial position.

General Fund

7.9 The above table shows that the level of reserves on the General Fund are now expected to remain at a sufficient level in the shorter-term due mainly to budget savings already identified to address the loss of central government funding. However, they are still projected to fall well below the minimum level of £1m by March 2016.

7.10 Although the projected budget deficit is reducing, the Council's budget over the next 5-years still depends on drawing down reserves each year. Clearly, the reliance on reserves to fund a budget deficit is not sustainable.

7.11 Therefore, in order to a achieve a sound and stable financial position, it is critical that the Council adheres to the time frame for delivering the next round of budget/efficiency savings by October 2011 in order that they can be built into the MTFP. It is noted that actions are already in place to achieve this.

HRA

7.12 The overall HRA reserve is projected to fall below the minimum level of £1/2m by 2014. This position is a lot more critical than previously estimated. Again it is noted, that the current HRA Business Plan is being reviewed to ensure that the HRA remains sustainable.

7.13 It is important that this work is completed by the planned date of June 2011. In addition, the details of the final self-financing proposals will need to be considered very carefully.

Risks

7.14 The Council's financial plan is subject to risk, where many factors such as government funding and interest rates for instance, are outside the control of the Council. In addition, demand for service improvements and new capital investment are likely to put further pressure on the current financial position.

7.15 The budget and projections included in the MTFP allow for known variations, some growth due to development, together with assumptions regarding public sector pay and grant settlements.

7.16 It is clear that the Council continues to face a tough period financially. Having been affected by a significant loss of central government funding, it is considered that this will continue to affect the financial stability of the Council.

7.17 This means that reviewing existing spending levels, considering alternative options and constantly striving for greater value for money continue to be as important as ever. Therefore, the recommendation regarding further budget/efficiency savings should be fully endorsed.

Consultation and Provision of Information

7.18 The information and proposals contained in this report, together with further details on where the Council spends its money, have been presented across the District. Specifically, this has been undertaken via:

- Local area forums
- Consultation with the Community and Voluntary Sector, including a Special Finance Committee on 24th January.
- Meetings with members of the local business community

7.19 In addition, the proposals have been subject to the Council's scrutiny process. A separate report by the Overview and Scrutiny Committee is included elsewhere on the Agenda.

8.0 <u>Financial Implications</u>

8.1 As detailed in the report.

9.0 <u>Corporate Implications</u>

9.1 There are no direct legal or employment implications apart from any considered in the report.

10.0 <u>Community Implications</u>

10.1 The proposed budgets and spending, provides the financial resources to enable all of the on-going services and Council priorities to be delivered to the local community.

11.0 Background Papers

11.1 The Government's Comprehensive Spending Review (October 2010) available at: http://cdn.hm-treasury.gov.uk/sr2010_completereport.pdf

11.2 The Government's Financial Settlement for 2011/12, available at: http://www.local.communities.gov.uk/finance/1112/grant.htm

11.3 Department for Communities and Local Government - Housing Subsidy Determination (and associated papers) 2011/12, available at: http://www.communities.gov.uk/publications/housing/hrasubsidydeterminations1112

11.4 Finance and Management Committee, 13th January 2011 – Detailed Budget Proposals and Analysis, available at: http://cmis.south-derbys.gov.uk/CmisWebPublic/Meeting.aspx?meetingID=1420