

BUDGET TARGETS 2020/21 AND THE DEVELOPMENT OF THE MEDIUM TERM FINANCIAL STRATEGY FOR 2020-2024

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| Head of Service/Contact: | Lee Duffy, Chief Finance Officer |
| Urgent Decision?(yes/no) | No |
| If yes, reason urgent decision required: | N/A |
| Annexes/Appendices (attached): | Annex 1 - Budget Forecast Annex 2 - Financial Modelling Annex 3 - Economic Indicators Annex 4 - Surrey Council Tax Charges Annex 5 - Key components of 2016-20 MTFS |
| Other available papers (not attached): | Budget Book 2019/20 |

Report summary

This report recommends budget targets for 2020/21 and provides a further update on the financial forecast and issues affecting the new four year financial plan.

Recommendation (s)

That the Panel recommends to the Strategy and Resources Committee:-

(1) The following overall budget target for 2020/21:-

- (a) estimates are prepared including options to reduce organisational costs by £544,000 in 2020/21 to minimise the use of working balances and maintain a minimum working balance of £2.5 million in accordance with the medium term financial strategy;**
- (b) that at least £290,000 additional revenue is generated from an increase in discretionary fees and charges, is based on minimum overall increase in yield of 3.0%, with the exception of car parking which is set at 6.0% as these charges are adjusted every two years;**
- (c) that a provision for pay award is made of £400,000 that allows for a 2% cost of living increase,**

(2) That further savings are identified for inclusion within the new Medium

Term Financial Strategy for 2020-2024 to reduce the Council's net operating costs by a minimum of £1,825,000 over the period 2020/21 to 2023/24;

- (3) That Capital Member Group seeks to maintain a minimum capital expenditure programme to control the use of capital reserves between 2020 and 2024, subject to an appropriate prioritisation of spend to save and externally funded schemes.**

1 Implications for the Council's Key Priorities, Service Plans and Sustainable Community Strategy

1.1 The Medium Term Financial Strategy comprises a supporting document to the Council's Corporate Plan.

1.2 The key components of the current Medium Term Financial Strategy 2016 – 2020 are attached at Annexe 5.

1.3 The Strategy and Resources Committee has agreed the following key service priority:-

“Produce a new Medium Term Financial Strategy with regard to the Fair Funding Review and report to Strategy & Resources Committee”

1.4 It is the Financial Policy Panel's role to advise the Strategy and Resources Committee on all matters relating to the budget and policy framework.

2 Background

2.1 The Financial Policy Panel has already received a report in the early stages of preparation for next year's budget and the review of the Medium Term Financial Strategy (MTFS):-

2.1.1 On 18 June 2019 the Panel agreed the preferred approach to carry out the 2020/21 budget review and the budget reporting timetable.

2.2 This report seeks the Panel's guidance on the corporate targets for preparing the 2020/21 budget and discusses the main issues faced in preparing the new Four Year Financial Plan and MTFS for 2020-2024.

2.3 The report covers:-

2.3.1 A review of the Council's financial standing;

2.3.2 The budget outlook for 2020/21;

2.3.3 An update of the ten year budget forecast 2020-2030;

2.3.4 Key funding changes during the next ten years (new homes bonus, localisation of business rates, welfare benefit changes and public sector pensions).

- 2.4 The report provides an updated estimate of the efficiency savings needed next year and the scale of total savings needed over the following three years.

3 Financial Planning

- 3.1 At its last meeting the Financial Policy Panel discussed the difficulty of planning in an environment with a high degree of uncertainty. The Government's future funding settlement for local councils remains unclear going forward with the outcome of the Fair Funding review and the Redistribution of Business Rates review still unknown and their impact for individual councils.
- 3.2 The Fair Funding Review had initially been expected to feed into a multi-year funding settlement for local authorities from 2020/21. However, on 9 August the Chancellor of the Exchequer, Sajid Javid, announced that a multi-year funding settlement will now be postponed until next year. Instead, the Treasury will conduct a one-year Spending Round for 2020/21, due to complete by the end of September 2019, although no exact date has been given for the announcement of any figures.
- 3.3 With existing funding streams at increased risk the Council has taken a prudent approach for financial planning, limiting the Council's reliance on funding from Government through retained business rates and New Homes Bonus Grant to fund the annual cost of providing services.
- 3.4 As outlined in the report Financial Planning 2020/21 to the Financial Policy Panel in June, a work programme has been agreed to assist in addressing the funding shortfall for the next Medium Term Financial Strategy 2020-2024.
- 3.5 The key features of the programme comprise:-
 - 3.5.1 A base review, this entails reviewing the year end position for 2018/19, identifying any potential savings, additional cost pressures and areas where savings can be developed. These will be used to update the financial plan.
 - 3.5.2 A 'Star Chamber' exercise where Service Heads will present options for their services on how savings to the Council can be generated over the next four years.
 - 3.5.3 Service Reviews to be undertaken over the next four years with the aim of improving efficiency, effectiveness and cost.
 - 3.5.4 Property Related Review – to realise cost reduction of Council operational buildings, increase income from investment properties and generate new receipts from surplus buildings/land.

3.5.5 Income Generation Review – to include analysis of charging powers and service utilisation and identify options for income generation.

4 The Council's Financial Position

4.1 The Panel has received a separate report on this agenda reviewing the level of revenue and capital reserves.

4.2 The increase in strategic reserves over the last four years are mainly as a result of one-off gains from New Homes Bonus Grant and Business Rates Pilot scheme. The levels of New Homes Bonus funding are in decline and over the next four years following the Fair Funding Review it is very unlikely that the Council will be in a position to be able to make further significant contributions to strategic reserves.

4.3 The level of strategic reserves are expected to be at £14.7 million by the end 2023/24, compared to £14.3 million anticipated at the end of 2019/20.

4.4 The projected level of strategic reserves includes an increase in the Property Income Equalisation Reserve of £1.7 million to meet the Council's objective to accumulate sufficient funds to cover the potential loss of one year's rental income at properties funded through borrowing, this is partially offset by a reduction in the other strategic reserves of £1.3 million.

4.5 A summary of the Council's forecast movement in reserves is as follows:-

| | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 |
|-------------------------------|---------|---------|---------|---------|---------|
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| General Fund Working Balances | 3,416 | 3,257 | 2,730 | 2,731 | 2,731 |
| Strategic Reserves | 14,324 | 14,906 | 15,263 | 14,972 | 14,731 |
| Capital Receipts | 2,626 | 2,076 | 1,626 | 1,276 | 1,026 |

4.6 The above forecast also shows a steady decline in the level of uncommitted capital receipts and by 2023/24 is expected to be just above the minimum agreed level of £1 million. This forecast also assumes an increase of £100,000 year on year in revenue funding for the annual capital programme to mitigate this and assist the Council in developing a sustainable capital programme

4.7 The following assumptions have been used in forecasting the position on reserves at the end of 2023/24:-

4.7.1 £700,000 annual capital programme requiring financing from either capital reserves or revenue.

- 4.7.2 £300,000 per annum of corporate projects reserve being used to fund revenue budget/schemes
- 4.7.3 £75,000 from the property maintenance reserve required to fund the annual backlog maintenance works.
- 4.7.4 £25,000 per annum from the insurance reserve used to finance costs within the revenue budget.
- 4.7.5 Annual contributions of £675,000 are made in 2020/21 and 2021/22 from the revenue budget to the property income equalisation reserve.
- 4.7.6 £2.5 million of the business rates equalisation reserve is used by 2023/24 to mitigate the impact of the fair funding review and potential NHS appeal.
- 4.8 In order to prepare the draft MTFS it is recommended that the policy on the minimum working balance is set at £2.5 million.
- 4.9 As discussed, there is no set formula for deciding on policy for a minimum level of working balance for the next four years but the following factors provide a context for the decision:-
 - 4.9.1 The Council's turnover is approximately £40 million including benefit payments and the balance would be approximately 5% of gross expenditure;
 - 4.9.2 The Council's turnover excluding benefit payments is approximately £20 million and the proposed balance would be approximately 10% of gross spend on services;
 - 4.9.3 The Council's net budget requirement (council tax and formula grant) is £8.5 million and the proposed balance would be approximately 25% of net expenditure.
- 4.10 The Panel's views are sought on an appropriate minimum working balance for the next MTFS.

5 Budget Outlook for 2020/21

- 5.1 The following comprises an analysis of the potential extra bottom-line costs the Council faces next year, and the steps needed to manage the budget position (i.e. to set a balanced budget with no use of the working balance). The figures are high level and they will be investigated further as part of the budget setting process. No detailed estimates have been prepared at this stage.

| Budget Deficit prior to Budget Savings Strategy | £000 |
|--|---------------|
| Budget deficit carried forward (planned use of working balance in 2019/20) | 0 |
| | |
| Forecast of Potential Cost Increases | |
| General Inflation (estimate based on unavoidable increases in specific budgets only, e.g. fuel and energy, contracts and business rates) | + 190 |
| Allowance for Staff Pay | + 400 |
| Increase in cost of waste collection | + 31 |
| Increase in provision for property maintenance | + 50 |
| Funding for Property and Regeneration Manager (funded from future income generation) | + 50 |
| Funding for projects within the capital programme | + 100 |
| Loss of funding from SCC towards Bourne Hall | + 80 |
| Reduction in Retained Business Rates (Baseline reset for 2020/21) | + 160 |
| Net prior year funding from collection fund | + 122 |
| Potential Budget Growth | 1,183 |
| | |
| Steps Needed to Address Budget Deficit | |
| Remove provision for Local Elections | -70 |
| Increase in dividend income from EEPIC (Council owned Property Company) | -100 |
| Increase income from interest on balances | -34 |
| Increased income from property, including acquisitions or reduced costs | -100 |
| Star Chamber savings or increases to income | -185 |
| Increase in Fees and Charges at an overall yield of 3% (6% for car parks) | -290 |
| Council Tax Increase – provisionally at 3% | -245 |
| Potential Budget Reductions | -1,024 |
| | |
| Required Use of Working Balance in 2020/21 after savings * | 159 |

- 5.2 The highest expenditure risks for next year where more detailed analysis is being carried out at an early stage in the budget process is:-

5.2.1 The growing costs of homelessness and temporary accommodation;

5.2.2 Delivery of efficiency savings targets included in the forecast.

5.3 There is also a further risk on delivering additional income from services and further reductions to grants and contributions received from both central government and Surrey County Council as they seek also to reduce.

6 Ten Year Budget Forecast

6.1 Annexe 1 comprises an update of the forecast budget position for 2020/21 (as set out above) along with an indicative forecast for the following nine years to March 2030.

6.2 The forecast indicates that a level of savings of £1.825 million is needed to achieve a balanced budget over the next four year financial planning period and would involve an annual saving of £0.544 million for 2020/21, broken down indicatively as follows:

| 2020/21 Budget Targets | £000 |
|---|-------------|
| Increase in dividend income from EEPIC (Council owned Property Company) | -100 |
| Increased income from property, including acquisitions or reduced costs | -100 |
| Star Chamber savings or increases to income | -185 |
| Further efficiencies or income to balance budget | -159 |
| 2020/21 Total Savings or Additional Income | -544 |

6.3 Without making savings the budget would move incrementally to a £1.8 million budget deficit by 2023/24. The general fund working balance would be fully utilised before that date.

6.4 The detailed forecast for the four years of the new Medium Term Financial Strategy at **Annex 1** is summarised in the following table:-

| | <u>2019/20</u> | <u>2020/21</u> | <u>2021/22</u> | <u>2022/23</u> | <u>2023/24</u> |
|---|------------------------------|----------------------------------|----------------------------------|----------------------------------|----------------------------------|
| | <u>Budget</u> <u>£000</u> | <u>Indicative</u> <u>£000</u> | <u>Indicative</u> <u>£000</u> | <u>Indicative</u> <u>£000</u> | <u>Indicative</u> <u>£000</u> |
| Net Expenditure on Committee Services b/f (before use of interest on Balances & BRER) | | 8,328 | 8,484 | 8,742 | 8,508 |
| Pay & Prices Increases | | 590* | 598 | 606 | 618 |
| Increases in Fees & Charges | | - 290 | - 210 | - 210 | - 216 |
| Policy Committee budget changes | | 161 | 150 | 150 | 250 |
| Changes to external funding | | 80 | 0 | 0 | 0 |
| Allowance for increased income from property | | -100 | -100 | -100 | -200 |
| Reduction in transfers to Property Equalisation Reserve | | 0 | 0 | -500 | 0 |
| Savings Target | | - 285 | - 180 | - 180 | - 180 |
| Forecast Net Cost (before use of interest) | 8,328 | 8,484 | 8,742 | 8,508 | 8,780 |
| Interest credited to General Fund | -96 | -130 | -175 | -240 | -270 |
| Funding to /from Business Rates Equalisation Reserve | -1,845 | 0 | -200 | -150 | -100 |
| Forecast Net Cost of Services | 6,387 | 8,354 | 8,367 | 8,118 | 8,410 |
| Retained Business Rates Forecast | 1,585 | 1,425 | 816 | 832 | 849 |
| Council Tax Income Forecast | 6,525 | 6,770 | 7,024 | 7,287 | 7,561 |
| Collection Fund Surplus / (Deficit) | -1,723 | 0 | 0 | 0 | 0 |
| Assumed Collection Fund Income (Formula Grant + Council Tax) | 6,387 | 8,195 | 7,840 | 8,119 | 8,410 |

* assumes annual pay increases limited to 2% and allows for unavoidable price inflation only

| | | | | | |
|--|----------|------------|------------|------------|----------|
| Forecast Budget Shortfall (required use of working balance) | 0 | 159 | 527 | - 1 | 0 |
|--|----------|------------|------------|------------|----------|

6.1 The forecast position is dependent on the detailed assumptions used and the ability of the Council to make the necessary savings.

6.2 The following factors have been used to prepare the forecast:-

| FOUR YEAR FORECAST: ASSUMPTIONS USED | | <u>2020/21</u> | <u>2021/22</u> | <u>2022/23</u> | <u>2023/24</u> |
|---|-------------|-------------------|-------------------|-------------------|-------------------|
| | <i>BASE</i> | <u>Indicative</u> | <u>Indicative</u> | <u>Indicative</u> | <u>Indicative</u> |
| | <u>£000</u> | | | | |
| General Inflation - prices | 9,500 | 2%* | 2% | 2% | 2% |
| Annual pay award | 11,000 | 2%* | 2% | 2% | 2% |
| Fees & Charges allowance: annual increased yield on discretionary charges | -6,600 | 3%** | 3% | 3% | 3% |
| Interest rate used | | 1.0% | 1.25% | 1.5% | 1.5% |
| Change in Retained Business Rates | -1,585 | -10.1% | -38.4% | 2.0% | 2.0% |
| Increase in Council Tax income | -6,525 | 3% | 3% | 3% | 3% |

** assumes annual pay increases limited to 2% and allows for unavoidable price inflation only*

*** increase to parking charges are applied every 2 years*

6.3 Assumptions have been made on potential significant changes to government financing as a result of the Fair Funding and the Business Rates Retention reviews and are discussed further below. These include:-

6.3.1 New Homes Bonus

6.3.2 Localisation of Business Rates

7 New Homes Bonus Scheme

7.1 The Council in recent years has benefited from the award of New Homes Bonus grant, based upon the number of new residential properties in the borough in the preceding year, with a supplement for affordable housing.

- 7.2 The methodology for this grant allocation was changed in 2017/18 by Government which resulted in a significant reduction in funding allocations in 2018/19. Originally the Council received a rolling 6 years of individual allocations; this was reduced down to 4 years from 2018/19 alongside a further reduction by only awarding funding for growth in homes above the 0.4% per annum baseline.
- 7.3 The amount of funding available from New Homes Bonus has diminished substantially over the last few years, in 2016/17 the Council received in excess of £2 million. With most of the current award made up from legacy payments there is a strong likelihood that this source funding could reduce even further in the future or be removed altogether as part of the Fair Funding Review.
- 7.4 Due to the future uncertainty regarding this grant the 2019/20 Budget approved by Council in February 2019 agreed that New Homes Bonus is no longer used as a source of funding for on-going services.
- 7.5 If the current scheme remains unchanged following the Fair Funding Review then the following grant is forecast over the next three years;

| | 2019/20 £'000 | 2020/21 £'000 | 2021/22 £'000 | 2022/23 £'000 |
|--|------------------|------------------|------------------|------------------|
| 2016/17 | 158 | | | |
| 2017/18 | 46 | 46 | | |
| 2018/19 | 219 | 219 | 219 | |
| 2019/20 | 21 | 21 | 21 | 21 |
| 2020/21 | | 21 | 21 | 21 |
| 2021/22 | | | 21 | 21 |
| 2022/23 | | | | 21 |
| Projected Grant (based on current scheme) | 444 | 307 | 282 | 84 |

8 Localisation of Business rates

- 8.1 The Government last year announced they would be undertaking a review of Retained Business Rates. The impact of the review remains unknown and in all likelihood will be delayed until 2021/22. However, the Council can still expect to see a reset of its Baseline position for 2020/21, which means that the benefit that the Council was receiving from the fund for being above its baseline will be removed. For the purpose of the forecast position it is assumed that the Baseline will be reset for 2020/21 and as a result reduce the funding receivable from retained business rates to £1,425k.
- 8.2 The impact of the Review is expected in 2021/22 and business rates income is anticipated to reduce by a further £625k which is the equivalent to the amount of negative RSG which was removed from the settlement in 2020/21 but likely to feature as part of the future settlement for business rates.
- 8.3 The forecast assumes these reductions are seen in 2020/21 and 2021/22, with the Council's subsequent share of retained business rates income for 2022/23 and 2023/24 increasing by 2%.
- 8.4 The Council maintains a Business Rate Equalisation Reserve to finance any fluctuations in its share of Business Rate income. The uncommitted balance on this reserve if the proposed transfer identified in the Review Reserves report takes place will be £500,000.

9 Economic Indicators

- 9.1 A table of the latest economic indicators is attached at **Annex 3**.
- 9.2 These statistics are issued by HM Treasury and the tables compare economic indicators available in July 2019 to those published one year ago.
- 9.3 The following table provides a summary of the main national economic issues that have an impact on the Council's budget at least for this year and next:-

| | Indicators | EEBC Budget Impact |
|------------------|---|--|
| Inflation | The Government's inflation target is 2%. Inflation (CPI) 2.0% in June 2019. HM Treasury collates independent average forecasts which for CPI are 1.8% for 2019 and 2.1% for 2020. | On prices the main concern is the level of increase on energy, fuel and index linked contracts. The level of increase will require additional funding to be allocated in 2020/21. The provisional forecast for 2020/21 includes a pay award settlement at 2% (the Government's target for |

| | | |
|------------------------------------|---|---|
| | | inflation). Currently CPI remains at 2%, however, this could increase in the next few months as a result of current economic uncertainty. |
| Interest Rates | The bank base rate remains at 0.75% and is only expected to increase slowly from 2020 onwards | Interest on Balances was budgeted at 0.8% for 2019/20. The forecast return on investments anticipates a gradual increase in returns up to 1.5% by 2023/24. |
| Household wealth and Demand | GDP growth was at 0.5% (Apr to June) Unemployment in UK at 3.8% (1.29m to May) The seasonally adjusted retail sales index is at 2.9% (June) | Benefits: The number of benefit applications has generally reduced in the last couple of years. However, with the implementation of Universal Credit this may account for some of the decrease in the number of applicants. Homelessness: The number of households in temporary accommodation is currently greater than last year (46 at the end of quarter one) and this trend for an increasing number of homeless households appears to be continuing into 2019/20. |

10 Financial Modelling

- 10.1 The ten year financial forecast includes assumptions as set out in paragraph 6.2 of this report.
- 10.2 The budget outlook estimates the level of savings needed based on a central case forecast. **Annex 3** provides an analysis of the impact of best case/worst case variations to the assumptions used.
- 10.3 Given uncertainties over the economy and public sector funding, significant variations may occur requiring careful monitoring and impact analysis throughout the budget process and the next four years.

11 Fees and Charges

- 11.1 The 2020/21 budget forecast assumes an additional yield on charges set by the Council generating £290,000 based on a minimum overall increase of 3.0% in total income, 6% for car parks as it was agreed that these charges will be adjusted every other year and no increases were applied for 2019/20.

- 11.2 Any shortfall in income will need to be offset by additional cost savings so that a balanced budget can be achieved.

12 Council Tax

- 12.1 The forecast assumes an increase of 3% per annum in council tax income. This level of tax increase would keep the council tax at the lower end of the Surrey Districts, consistent with the council tax policy.
- 12.2 The current Band D for the Borough is £198.36. The Borough's council tax is benchmarked against the other Surrey District council tax levels in **Annex 4**.
- 12.3 Although the forecast is based on a 2.99% increase options can be prepared for higher or lower levels of council tax. For each 1% increase the gain is £63,000 per annum. The cumulative effect of any variations to council tax increases need to be taken into account in the forward projections.
- 12.4 Currently central government has set a cap on the percentage increase allowed. For this Authority an increase of 3% or above would require a referendum to be held.

13 Capital Programme

- 13.1 The capital programme agreed in February 2019 can be found on page 78 of the Budget Book 2019/20.
- 13.2 The Strategy and Resources Committee (July 2019) agreed that schemes totalling £4.91 million be carried forward and added to the £1.11 million programme approved for 2019/20.
- 13.3 The capital programme review for 2020-2024 is under way. The Capital Member Group held their first meeting earlier this month. Scope for capital investment will be restrained taking into account the revenue budget position, the reducing level of capital reserves and the limited scope for capital disposals at the current time.
- 13.4 A separate report on the agenda reviews the level of capital reserves, but the forecast position shifts funding of the Council's core capital programme away from use of diminishing capital receipts to being financed through the revenue general fund. By the end of 2023/24 £0.5m of the estimated £0.7m annual capital programme is expected to be financed from revenue.
- 13.5 It is anticipated that the core programme will be restricted to essential investment in existing assets and investment in projects that will reduce future running costs or raise additional income (spend to save schemes) however there is scope for external funding of schemes and in particular the use of specific grants such as the disabled facility grants.

14 Proposals

- 14.1 The proposals for the Strategy and Resources Committee are set out in the recommendations of this report.
- 14.2 The Panel is requested to advise whether any changes are needed to the budget strategy or the charging assumptions used in setting the budget target for 2020/21.

15 Financial and Manpower Implications

- 15.1 Decisions on a pay settlement for April 2020 are not required prior to the budget being agreed however resource constraints will need to be taken into account in any pay award.

16 Legal Implications (including implications for matters relating to equality)

- 16.1 The Council will continue to fulfil its statutory obligations on all services provided.

17 Sustainability Policy and Community Safety Implications

- 17.1 The Council's new Medium Term Financial Strategy will support the Council's new Corporate Plan, including the sustainability and community safety priorities therein.

18 Partnerships

- 18.1 None for the purposes of this report.

19 Risk Assessment and Conclusions

- 19.1 This report covers budget targets for 2020/21, taking into account the financial forecast for the next ten years. The report also considers the major risks to and uncertainties over the Council's finances over the next four years.
- 19.2 2020/21 will comprise the first year of a new four year financial plan. In setting budget targets the Panel is also being asked to provide advice on the development of the new Medium Term Financial Strategy.
- 19.3 Based on the assumptions used, the forecasts indicate that further significant budget reductions are required in the region of £544,000 in 2020/21 and £1.825 million over the next four financial years after allowing for price increases, charging increases and government grant cuts.

- 19.4 The budget strategy involves increasing income and reducing expenditure in regards to property, continuing to deliver efficiency savings and generate extra service income whilst reviewing service levels so that service costs can be reduced as needed to achieve a balanced budget year on year.
- 19.5 The budget strategy also requires limiting the reliance on funding from government such as retained business rates and specific grants for funding council services.
- 19.6 Following the review of the Corporate Priorities, service plans should facilitate a reduction in the net cost of providing services over the next four years.
- 19.7 The greatest financial risks continue to be the increase in homelessness expenditure and the impact of further benefit reforms. The main corporate finance risks are the level of funding reductions as a result of the Fair Funding Review.
- 19.8 The budget position for next year will be reassessed later this year when detailed estimates have been prepared.

Ward(s) affected: (All Wards);

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