Deputy Chief Executive's Office

Dean Taylor

Members of the Overview and Scrutiny Committee:

AM Atkinson, PL Bettington, WLS Bowen, MJK Cooper, PGH Cutter, EPJ Harvey, MAF Hubbard, RC Hunt, TM James, Brig P Jones CBE, JLV Kenyon, JW Millar (Deputy Chairman), R Preece, SJ Robertson, P Rone, A Seldon (Chairman) and PJ Watts and Statutory co-optees: Mr P Burbidge, Miss E Lowenstein, Mr T Plumer and Mr P Sell.

Your Ref: N/A
Our Ref: Monday 16 January 2012
Please ask for: Tim Brown, Committee
Direct Line: Manager (Scrutiny)
Fax: 01432 260239
E-mail:
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11 January 2012

Dear Councillor,

Overview and Scrutiny Committee - Supplementary Report

Please find attached a supplementary report that was not available prior to the publication of the agenda for the forthcoming meeting (Monday 16 January 2012, at 10.00 am). Please bring these papers to the meeting.

8. BUDGET UPDATE 2011/12

To seek Overview and Scrutiny Committee's view on the budget for 2012/13 and the principles underlying the Medium Term Financial Strategy (MTFS).

Yours sincerely,

Tim Brown, Committee Manager (Scrutiny)

enc.

cc. Members and officers in receipt of Overview and Scrutiny Committee papers

Herefordshire Council

MEETING:	**CABINET**
DATE:	**19 JANUARY 2012**
TITLE OF REPORT:	**DRAFT FINANCIAL STRATEGY AND BUDGET 2012/13**
PORTFOLIO AREA:	**CORPORATE SERVICES AND EDUCATION**

CLASSIFICATION: Open

Wards Affected

County-wide

Purpose

To propose the draft financial strategy for 2012/13 to 2015/16 that includes the 2012/13 budget for approval by Council on 3 February 2012.

Key Decision

This is not a Key Decision.

Recommendation

THAT Cabinet recommends to Council on 3 February 2012

(a) Approval of the Medium Term Financial Strategy (MTFS) shown in Appendix A, which includes the 2012/13 budget and Treasury Management Strategy and Policy Statement;

(b) Approval of a freeze of Council Tax for 2012/13 at 2011/12 levels; and

(c) Approval of the Capital Programme outlined in paragraph 67 of the report.

Key Points Summary

- Cabinet has recommended that Council accepts the 2012/13 Council Tax freeze grant and does not increase its level of Council Tax.
- The Council will set its Council Tax on 2 March 2012. This must be based on a balanced budget. It cannot budget for a deficit.
- The Council continues to be affected by the reducing level of central government funding.
- The 2012/13 net budget total is **£143.359m** excluding schools funding.

Further information on the subject of this report is available from
David Powell, Chief Officer: Finance and Commercial Services on 01432 383518

Alternative Options

1 A balanced budget for 2012/13 is proposed and summarised in the Financial Resource Model (FRM) in the attached MTFS. It incorporates inflation, service pressures and other spending requirements. Funding has been identified from within Council Tax, Formula Grant, service efficiencies and reductions.

Reasons for Recommendations

2 The Council has a legal obligation to set a balanced budget as required by the Local Government Finance Act 1992. The proposed MTFS shown in Appendix A provides a financial planning framework for the next four years.

Introduction and Background

3 The Cabinet is requested to consider the budget proposals set out in the MTFS in order to make a recommendation to Council for setting the 2012/13 revenue budget based on holding Council Tax at current levels.

4 The provisional local government settlement was announced on 8 December 2011. The key component is the Formula Grant, which includes Revenue Support Grant and redistributed business rates, which is set at £54.462m (£56.615m after including council tax freeze grant). This is a £5.7m cash reduction on the amount received in 2011/12 and it is unlikely this will change when the final settlement is published in late January 2012.

Considerations

Provisional Local Government Settlement 2012/13

5 Local government will enter the 2012/13 financial year without certainty about the funding position for 2013/14 onwards. This is because CSR10 announced in October 2010 only provided a finance settlement for two years (2011/12 and 2012/13). However, the council's assessment of funding for budget planning purposes assumes at least 10% reduction over the 2013/14 to 2015/16 period. A more fundamental review of local government funding is anticipated from 2013/14 so outline assumptions are used at this stage.

6 The provisional local government settlement for 2012/13 was announced on 8 December 2011. The formula grant (Revenue Support Grant and redistributed business rates) remains unchanged from the figure previously announced of £54.462m (before the council tax freeze). This compares to £60.191m in 2011/12, a cash reduction of £5.7m (9.5%). Some additional funding is provided for in the provisional 2012/13 settlement:

a. £1.5m social care funding within formula grant;

b. £2.1m of funding for the 2011/12 council tax freeze. This will cease after 2014/15; and

c. £2.3m NHS funding to support social care.

7 The New Homes Bonus match funds the additional council tax raised for new homes and empty properties brought back into use. The scheme commenced in April 2011 and is paid for six years. Herefordshire was awarded £591k per annum for 2011/12 and has been provisionally awarded £824k for 2012/13 (paid for six years from 2012/13). The council's financial model now reflects the national top slice expected from 2013/14 that will reduce the allocation.

8 The Department for Education has indicated that Dedicated Schools Grant (DSG) remains at £4,723.65 per pupil.

Autumn Statement – November 2011

9 On 29 November 2011 the Chancellor of the Exchequer made his Autumn Statement to the House of Commons updating MPs on economic and fiscal forecasts for the UK economy. Key points for councils were;

- The Chancellor confirmed that there would be no change to the figures already announced in the 2010 Spending Review. The Chancellor also stated that he had set new Expenditure Totals for the end of the spending review period: 2015/16 and 2016/17. Over these two years, the Total Managed Expenditure is set to fall by 0.9% a year in real terms, excluding one-off investments in infrastructure announced in the Autumn Statement.

- The Statement reiterated the Government's offer of a one-off council tax freeze grant in 2012/13 "to help with the rising cost of living", which had been announced previously.

- The Chancellor announced an extra £1.2bn spending on schools. £600m will help the local authorities with the greatest basic need for schools places and is hoped to fund an additional 40,000 places. The remaining £600m will support reforms and build 100 additional Free Schools – including Maths Free Schools for 16-18 year olds. He also announced that the number of childcare places for deprived 2 year olds will double from 130,000 to 260,000.

- Following the 2-year pay freeze there will be a 1% cap on public sector pay. There will also be a review of regional pay.

- The small business rate relief "holiday" was extended for a further 6 months to 1 April 2013.

- 2012/13 business rates are to be up-rated in line with September RPI at 5.6%. Businesses will be given the opportunity to defer 60% of the increase to be repaid in the following 2 years.

- An extra £1bn was announced for the Regional Growth Fund over the remaining Spending Review.

Council Tax Freeze Grant for 2012/13

10 On 3 October 2011 the Chancellor of the Exchequer announced that the Government will pay a grant to authorities which freeze their council tax for 2012/13. This grant is for one year only.

11 By accepting the grant Herefordshire Council will freeze council tax bills for a second successive year. However, a careful approach is needed in order to manage the consequences for council tax and budgets in subsequent years as the grant will only fund one year of grant payment at 2.5%.

12 The grant covers 2012/13 only and is therefore very different from the funding for the 2011/12 council tax freeze where the government will pay the grant for the four years of the spending review (up to and including 2014/15).

13 The grant on offer covers the equivalent of 2.5% increase in council tax (this equates to £2.16m for Herefordshire Council). The grant for Police and Fire and Rescue Authorities is 3%. The grant does not cover parish and town council precepts.

14 Payment to the council will be made by a single amount in March or April 2012 and will be made as soon as the council confirms it will freeze the 2012/13 council tax. For Herefordshire this would follow council tax setting. The grant is not ring fenced and can be used for any purpose. It could also be carried forward if not fully used in 2012/13.

15 As indicated, accepting the grant rather than increasing council tax by the same amount means losing the "base" effect of a 2.5% council tax increase. Therefore it is proposed, subject to final Council approval, to use the grant as a one off source of funding for transformation (including Root and Branch reviews – see below) and budget contingency in 2012/13. The approach to the use of the funding will be developed before the end of March but it will be based on supporting transformation to enable sustainable budget reductions to be made, with a particular emphasis on Adult Social Care.

Grants for 2012/13

16 In 2010 the government announced a significant reduction in the number and value of grants that affected 2011/12 and to a lesser extent 2012/13. The allocations for 2011/12 and 2012/13 (excluding Council Tax Grant and Dedicated Schools Grant) are as follows:

List of Grants	**2011/12 £000**	**2012/13 £000**
Early Intervention Grant	6,501	7,097
HCTB Admin	1,228	1,177
Music grant	263	236
Community Safety	158	80
Home to school transport	435	540
Lead Local Flood Authorities	130	200
Learning Disability	3,657	3,738
Preventing Homelessness	225	225
TOTAL	**12,597**	**13,293**

17 In 2011/12 £13.5m of specific grants and Area Based Grant were moved into formula grant, but reduced to an estimated £10.8m, leaving a funding shortfall of £2.7m. A further £932k reduction in these grants is estimated to be included in the Formula Grant reduction in 2012/13. The above shows an increased total compared with 2011/12 but this comes with additional responsibilities and in some cases increases will be passported to other bodies.

18 The Council Tax and Dedicated Schools Grants are the only ring fenced grants. As a result this gives greater flexibility when using the grants outlined above.

19 In 2012/13 the Early Intervention Grant increases by £596k but the additional amount is to

cover the responsibilities to provide pre-school places for vulnerable two year olds.

Budget and Policy Process

20 The 2012/13 budget process has seen greater alignment between policy and budget setting. This builds on the process that commenced in the previous year and led to a series of star chambers in late 2011. The star chambers had the following aims:

a. To sign off the savings agreed in 2010 as part of the two year process;

b. To seek additional savings to meet the emerging gap resulting from the Council Tax freeze grant for 2012/13; and

c. To test the requirement for additional funding built into the current financial model.

21 As part of the overall process the following core principles set out what the council stands for and what residents can expect of it.

PRINCIPLE	IMPACT
Valued Services	• *Focusing on our priorities & what matters to people, stopping things we don't need to do*
Reducing Bureaucracy	• *Less regulation and red tape, smaller local government; right first time delivery*
Supporting the Vulnerable	• *Targeting resources on individuals, families, communities at risk or disadvantaged; early intervention & prevention; a shift in social care provision*
Value for Money	• *Reducing the pay bill; third party spend savings; smarter delivery; cutting costs*
Local Delivery	• *Devolution to parishes and the VCS, local decision making; working through 9 localities*
Personal Responsibility	• *Self reliance, people and communities helping themselves, behavioural change; increase in personalisation*

22 It is important to note that Cabinet of 15 December 2011 agreed to recommend to Council that the 2012/13 Council Tax Freeze Grant announced on 3 October 2011 by the Secretary of State be accepted, which means, subject to Council approval, there will not be an increase in council tax in 2012/13. However, the one year nature of the funding means the permanent ongoing increase that would have occurred from the assumed 2.5% increase in Council Tax is foregone. As a result the Cabinet's policy is to use this as "one off" funding split between transformation (£1.2m) and budget contingency (£1.0m).

Income Generation

23 During 2009/10, the Council generated £18.1m through fees, charges and sales which was 4.7% of total gross revenue expenditure.

24 According to benchmarking analysis undertaken by the council and Price Waterhouse Cooper, in a number of specific expenditure areas (e.g. pest control, highways planning, water safety),

the council performs well on recovery relative to nearest neighbour authorities. Overall, though, the council has the lowest recovery rate out of 15 comparators.

25 The intention is to become a median performer in terms of income recovery, which would mean generating approximately £2.78m of additional net income per year. A ‘stretch’ target of £12.43m has also been identified, representing average upper quartile performance.

26 The 2011/12 budget includes £712k to be delivered through increases in existing income and the development of new income streams within directorates.

27 A set of Charging Principles for the council has been agreed by Cabinet, and a process for approving new income proposals has been put in place by the Commercial Board in response to these.

28 Cabinet approved three ‘quick win’ income proposals in June 2011. These covered car parking, pre-application planning advice and school transport. There are a number of further income projects at varying stages of development across the authority.

29 The Overview and Scrutiny Committee have also been tasked with “undertaking a review to identify options for the development of budgetary policy to support further income generation”. This will influence the outcome of the PwC work and the council’s medium term plan.

Budget Setting Principles

30 The MTFS, attached to this report, includes the council’s financial model. This indicates the variations to the budget including amounts to meet pressures as well as compensating savings. The key points are as follows:

a. Inflation: the model includes net inflation of £2.35m.

b. Additional funding for Adult Social Care: the council will passport to Adult Social Care the £1.48m included in the formula grant along with funding from the NHS included in the CSR10 announcement.

c. Further savings from the Shared Services programme amounting to £571k are included for 2012/13.

d. Change management: the budget includes £1.0m to support costs associated with staff reductions. If the government permits capitalisation of such costs in 2012/13 (as it did in 2011/12) the council will make a case to take advantage of this approach.

e. Council Tax: the 2012/13 budget includes use of the one year Council Tax Freeze Grant announced in 2011. This means for the second year council tax will not be increased. Future years assume 2.5% increase.

f. Council Tax Freeze Grant: the 2012/13 amount on offer from central government will be used to support transformation activity (£1.2m) and the balance of £1.0m will be used as budget contingency.

g. Pressures: the budget includes £907k for contract inflation; £785k for service and demographic pressures and £544k for statutory changes. In total the budget includes £2.236m of additional funding to support pressures.

Financial Management and Reserves

31 A key part of the budget process is to ensure the council has appropriate levels of reserves especially at a time of continuing financial challenge. Over the medium term it is proposed that the council will put in place a budget contingency.

32 The current level of the general reserve is £6.3m representing 4% of the net budget. Whilst the policy is for a general reserve of 3% it is considered prudent to use any amount in excess of 3% to fund a budget contingency reserve.

33 The Council holds a variety of reserves some of which relate to schools. In total the overall level of reserves will be approximately £16m on 31 March 2012 but within this total it is assessed £8.6m will be available for corporate use. These include the General Fund (£6.3m), Waste Disposal Reserve (£1.9m), Whitecross PFI Reserve (£0.3m) and Insurance Reserve (£1.0m).

2013/14 Onwards

34 The funding position for 2013/14 onwards is much less certain. Currently the government is consulting on a proposal that will see councils retain business rates for their area. This is a significant change to the current arrangements where Herefordshire collects business rates on behalf of the government and receives a formula grant in return.

35 The proposed changes give councils some local control and provide an additional incentive to support economic growth. However local changes to collection rates can lead to income fluctuations in any year. Herefordshire gains from the current system and currently gets more funding through the formula grant than it collects in business rates. Herefordshire will need to ensure the “base” position supports the current level of funding in order to avoid additional financial pressure.

36 In 2013/14 local government will also see a significant change to Housing and Council Tax benefits. Housing Benefit will become part of the new single universal credit. Council Tax benefit will be funded by a specific grant paid to Unitary and District Councils. The amount paid will be subject to a 10% cut compared with 2012/13 levels of funding. Furthermore, those viewed as “vulnerable” by government regulations will receive a greater proportion of the overall grant than at present.

Directorate Budget Proposals

DIRECTORATE	ORIGINAL £’000	REVISED £’000
Corporate	**1,191**	**1,256**
Peoples	**3,500**	**4,324**
Places	**1,092**	**2,170**
Council Wide Initiatives	**240**	**1,554**
TOTAL	**6,023**	**9,304**

Corporate Services Directorate

37 The Directorate has identified total savings for 2012/13 of £1.256m.

38 The Directorate's savings plan for 2012/13 includes £571k further savings from Shared Services. The majority of which will be achieved through the contract arrangements with Hoople Limited.

39 There are also savings of £302k through further measures to reduce the pay bill across all services along with increased income from Charging Reviews in the Diversity and Registration services of 33k.

40 Other savings for the Directorate are as follows:

- Non-pay inflation across most services where contract inflation is not already committed, totalling £350k. Non-pay inflation has only been held back to meet committed pressures on ICT contracts. Root and Branch Reviews within Customer Services and Support Services are expected to achieve a further £250k.

Places Directorate

41 The Directorate has identified savings for 2012/13 of £2.17m. This is in addition to managing over £500k pressures in relation to contract inflation and new government initiatives, such as introduction of Neighbourhood Planning and Enterprise Zone.

42 Contract savings of £500k are expected through negotiations with Amey in relation to extending the current Managing Agent Contract beyond September 2013 along with savings from the FOCSA contract of £200k per annum by discontinuing the free provision of black sacks, although this is not be realisable until November 2012.

43 There is agreed reduction in Management Fee to partner organisations, Halo, Courtyard and Hereford Futures of 10%.totalling £173k, these fees have been reduce by 5% in each of the previous two financial years.

44 There is an expected increase in charges of £389k across the Directorate in line with the Charging Review, which includes increasing Car Park Fee income by £200k.

45 The balance of savings for the Directorate is being made from service efficiencies across all services, including £750k from service reviews. These are:

- Cultural Services £150k
- Regulatory Services £200k
- Transport £100k
- Community Protection & Parking £100k
- Provision of Public Toilets £200k

Peoples Directorate:

(a) Children's Services

48. The Directorate has identified savings of £4.32m. This is in addition to managing pressures such as £1.459m in Safeguarding services, due to the growth in child protection and looked

after children, plus other service pressures of £0.593m. The Children's Services budget was substantially reduced in 2011/12 as a result of cuts in both base budget and grants. Significant cuts were actioned across all service areas except for children's safeguarding services (which continue to experience increasing demand).

49. The savings are anticipated to be delivered through a combination of:

- restructure savings (full year effect of 11/12 staffing cuts) £591k,
- increases in grants confirmed of £776k,
- service reconfiguration yielding £421k across youth, connexions and children's centres,
- contract reductions of £235k,
- other early years savings of £150k,
- use of transformation fund £190k, targeted safeguarding savings of £150k,
- schools transport savings of £220k. The balance is expected to be delivered across a range of services with potential additional staffing cuts which have yet to be confirmed.

(b) Environmental Health, Trading Standards and Public Health

50. The Directorate has identified savings of £289k; this will be delivered through a combination of:

- service restructure which has been undertaken,
- increasing income budgets based upon maximum acceptable charges; and
- cutting non-essential expenditure.

51. The service will also operate with a shadow public health budget in 2012/13 in preparation for the budget transfer from 1st April 2013.

(c) Adults Services

54 The 2012/13 budget for adult services will see a £1.4m net increase compared to 2011/12 which is a result of additional funding from central government to support social care pressures. In order to achieve a balanced budget however, the Directorate has identified savings, efficiency and transformation schemes of £7.956m. This is to address medium term financial strategy required savings of £2.5m and this is in addition to a brought forward funding shortfall of £6.4m and 2012/13 demographic pressures of £3.6m. Mitigation by the additional funding streams and use of NHS monies for transformation has resulted in the net savings plan.

55 Given the scale of the cost challenge in Adult Services, consideration has been given to altering the threshold for adult social care services to critical. As this would be counter to the principle of early intervention, and unlikely to lead to cost reductions in the longer term, there will be no change to the eligibility criteria, which will therefore remain at substantial and critical needs.

56 Other measures to achieve a balanced budget have been considered including an increase of the threshold to Fair Access to Care Services to critical, rather than substantial and critical and not to award inflation increases to providers. However, following consideration, it has been decided that both would be counterproductive and not in the interests of service users in Herefordshire. Neither action would create sustainable service and budget positions and have therefore been discounted from these budget proposals.

57 The focus in the savings proposals is on transforming and re-shaping how services are provided with emphasis on reducing demand by creating greater independence. Through

different approaches to care. Transformation initiatives which will deliver the savings required are:

- reablement, enablement and substantially increasing the use of assistive technology
- reducing residential care by supporting people to live independently,
- creating a more vibrant market to offer greater choice and control to service users
- increased charges and removal of subsidies
- making better use of existing contracts and gaining better value for money from commissioned services.

58 To be able to achieve this investment of circa £1.4m is required which will support both health and social care to reshape supply from traditional `bed based` models of care.

59 A schedule of directorate savings is in Appendix A.

Schools Budget Settlement

Academies

60 The adjustments for Academies' funding have not changed from those previously announced However, the Department for Education, in consultation with the Secretary of State for Communities and Local Government, has been reviewing the amount and distribution of the funding transfers from local government for 2011/12 and 2012/13 to reflect the responsibilities transferring from them when schools convert to academies. No final decisions have yet been taken regarding the amount and distribution of these funding transfers.

61 For 2012/13 the top-slice from Formula Grant will remain at £265m, but a new methodology will be used to calculate individual authorities' contributions. Where this methodology suggests authorities have had more taken away than they should they will receive a specific grant. There will be no adjustment where the calculation suggests that an authority should have contributed more.

Schools and Children's Services funding

62 The Department of Education (DfE) made a separate announcement on Dedicated Schools Grant (DSG)and Pupil Premium;

- DSG is to be same flat cash per pupil, the rate therefore remains at £4,723.65 per pupil – so no increase in pupil funding for any authority
- The Minimum Funding Guarantee remains at (minus) 1.5% - as expected
- The spend on the pupil premium will double to £1.25bn. This is as expected.
- The pupil premium is to be £600 per free school meals pupil and Looked After Children and £250 for service children (up £50 from £200). The basis for payment has been widened so that it includes pupils who have ever had free school meals within the last 6 years. This will widen eligibility by approximately 30% and hence reduces the payment rate per individual pupil.

63 As expected there will be no uplift in DSG for 2012/13. It will continue to be paid at the same rate as in 2011/12 i.e. £4,723.65 per pupil. DfE have not provided an overall total and expect councils to work to their own estimates. Based on the September pupil count we now estimate 22,600 pupils i.e. a reduction of 117 pupils. Final pupil numbers will be confirmed in late February following the 2012 pupil census. Estimated DSG for 2012/13 is:

2012/13 Estimated Allocations	**£m**
DSG (22,600 pupils at £4723.65 per pupil)	106.75
TOTAL DSG 2012/13	**106.75**

64 The Schools Forum has already consulted on proposals to address the pressures within the DSG and will be making recommendations to the Cabinet Member in the light of the settlement.

Proposed Capital Programme

65 The Joint Capital and Asset Management Strategy agreed by Cabinet on 16 December 2010 sets out capital priorities and plans as well as how these link to strategic objectives.

66 The strategy listed a number of schemes that are priorities within the Joint Corporate Plan (JCP) and confirmed that if they continue to encapsulate the Herefordshire Public Services (HPS) Vision they could be funded as resources become available and are identified in coming years. These included a number of schemes that remain priorities. There is a key link between the strategy and the HPS strategic aim of "Herefordshire will be a place where people, organisations and business working together within an outstanding natural environment, will bring about sustainable prosperity and well being for all".

67 The strategy includes a number of additional key schemes. These are:

- Broadband – Herefordshire is one of four pilot areas identified that has received government funding. It is a requirement that the council match funds the programme and £6m will be made available.

- Hereford Futures – Hereford has been identified as a regional growth point and planning permission has been granted for a relief road as part of the overall package of infrastructure to facility and enable growth to take place. The relief road will also enable the bringing forward of new homes in partnership with Sanctuary Housing. The estimated cost of the overall scheme will be £27m for the relief road. It is proposed that this scheme is included and therefore funding decisions can be made to enable to council to lock in low rate funding, as the long term savings from borrowing sooner rather than later, may not be available if further postponed. It should be noted that the overall funding needed will be confirmed in 2012 and appropriate contributions will be sought from developers and other funding sources.

- The provision of a replacement Archives facility is required if Herefordshire is to continue to hold its county records. If a facility is not provided there is a likelihood that the county's historical records will need to be moved outside of Herefordshire. It is also appropriate to bring together modern records provision with the archives facility and so an overall facility is proposed up to a maximum capital cost of £6.0m.

- Stretton Sugwas Landfill: this is a £70k scheme to provide routine replacement of infrastructure.

68 The capital programme also includes a budget of £1.0m for repairs to Garrick House car park. These will ensure it continue to provide income and parking capacity for those shopping in Hereford City Centre.

69 In addition the Government supports capital investment through the allocation of grants. This approach replaces the previous supported borrowing model. Known grant funding allocations for 2012/13 are:

Local Transport Plan

- This has been reduced by a further 5% to £10m for 2012/13 split between integrated transport and capital maintenance allocations. Indications are this funding will fall further to £9.8m for 2013/14 and 2014/15.

- Hereford submitted a successful application, (Destination Hereford), for capital funding from the Local Sustainable Transport Fund, for sustainable transport initiatives in Hereford. £3.2m of grant funding is expected to be spent between 2012/13 and 2014/15 on improving Broad Street and providing the non-motorised connection between the city centre and Rotherwas.

Schools Capital

- There have been further substantial changes in the allocation of schools capital funding for 2012/13 due to a number of Herefordshire's schools converting to academies in 2011/12 and changes to the formula mechanisms that the DfE use to allocate capital grant funding.

- The total allocation for maintenance and basic need has reduced by 46% from an allocation of £4.8m in 2011/12 to £2.6m in 2012/13. Capital maintenance funding has been reduced by £0.9m; a separate funding pot is available for academies to bid for funding. Basic need funding has reduced by £1.3m as a result of funding formula changes from allocations being based on pupil growth and capacity in 2012/13 as opposed to being based on pupil growth alone in 2011/12. Further basic need funding available to central government is yet to be allocated. These allocations will be announced in the New Year along with the results of the priority school building review and response to the capital review carried out earlier in the year.

Adult Social Care

- The Department of Health has announced funding of £0.46m towards personalisation, reform and efficiency in adult social care in 2012/13.

Other Capital Grants

- Herefordshire has been selected as one of four pilot schemes to deliver superfast broadband to rural areas in Herefordshire and Gloucestershire, the procurement process is underway with the successful provider expected to be announced in May. The scheme is to be funded through grants from BDUK, Gloucestershire and corporate match funding.

- Herefordshire Council will receive £1.5m from the Regional Growth Fund for a new Marches Redundant Building Grant Scheme covering the 3 local authority areas in the Marches Local Enterprise Partnership (Herefordshire, Shropshire and Telford & Wrekin).

- Capital grant applications for funding towards the Masters House in Ledbury are to be confirmed, if successful this will enable the completion of the desired scheme.

70 The following summarises funding for the capital programme up to and including 2015/16:

	2012/13	2013/14	2014/15	2015/16
Directorate	**£'000**	**£'000**	**£'000**	**£'000**
People's Services	12,828	-	-	-
Places & Communities	17,591	16,917	10,842	-
Corporate Services	4,351	12,257	-	-
Funding to be allocated	4,260	11,200	11,492	6,213
Contingency	*332*	*330*	*283*	-
TOTAL	**39,362**	**40,704**	**22,617**	**6,213**
Funded by				
Prudential Borrowing	11,905	23,787	11,775	6,213
Capital receipts reserve	465	70	-	-
Grants and contributions	26,992	16,847	10,842	-
TOTAL	**39,362**	**40,704**	**22,617**	**6,213**

Equality and Human Rights

71. In demonstrating "due regard" in our decision making process, we will ensure that individual directorates and service areas assess the potential impact of any proposed changes that are as a consequence of budgetary constraints, leading to fairer, transparent and informed decisions being made.

Financial Implications

72 These are set out in the report.

Legal Implications

73 Local authorities must decide every year how much they are going to raise from council tax. They base their decision on a budget that sets out estimates of what they plan to spend on services. Because they decide on the council tax before the year begins and can't increase it during the year, they have to consider risks and uncertainties that might force them to spend more on their services than they planned. Allowance is made for these risks by:

- making prudent allowance in the estimates for services; and
- ensuring that there are adequate reserves to draw on if the service estimates turn out to be insufficient.

74 Local government legislation requires an authority's chief finance officer to make a report to the authority when it is considering its budget and council tax. The report must deal with the robustness of the estimates and the adequacy of the reserves allowed for in the budget proposals, so members will have authoritative advice available to them when they make their decisions.

Risk Management

75 The position outlined in the report indicates the state of public finances means a reducing funding envelope for local government. This creates a number of additional risks to those normally associated with any budget setting process. The following lists specific risks:

a. Directorate Savings: the loss of funding in 2012/13 requires a significant level of savings. There is a risk of slippage should unforeseen delays occur. The use of the £1.0m budget contingency will assist along with using anything in excess of 3% on the general fund reserve as a budget contingency reserve. Directorates' plans for delivery of savings will need robust management, and action plans to ensure delivery. Contingency plans will form part of the process.

b. Local Government Resource Review: 2013/14 will see one of the most significant changes to funding for local government. The proposal to allow councils to retain business rates rather than contribute to the national pool could create risk if the "base" level is set too low by central government. Central government will continue to control the level of business rate increase.

c. Treasury Management: the council has significant treasury management activity covering borrowing and investment. The current financial climate means this area plays an important part in resource delivery for the council. The decision to refinance existing borrowing and take on additional requirements will need to be timed to take advantage of opportunities provided by historically low interest rates.

d. Income: the council's budget is supported by income. The level of income receipt could be affected by factors such as the economic climate. The council's review of income and charging levels will need to play an appropriate part delivering the balanced budget.

Consultees

76 Herefordshire Public Services set out to ask local people for their views on funding priorities so that their feedback could help it to begin to plan how its budget should be used in the future. With current pressures on funding being experienced by public services nationwide, it wanted to explore a new way of engaging with the population at an early stage in the process. As a

result, a series of 10 public events were held across the range of localities in the county during November and December 2011, attended by over 250 people in total. Alternatively, people could give responses through an on-line questionnaire.

77 The consultation included four topic areas, on which people were asked a series of high-level questions about general spending principles on which each could cast their vote using an electronic hand-held device. Each section was first introduced by providing some contextual information. Questions were asked concerning finance, adult social care, clinical commissioning of healthcare, and health and wellbeing. This was followed by an opportunity for people to write further comment for each of the four topic areas, and to ask questions of the presenters. The public engagement exercise asked a series of questions and the headline responses are as follows:

a. Overall 54% agreed with prioritising funding for services for vulnerable people.

b. Overall just fewer than 60% of people agreed with the Council not providing some services to protect and develop others; 21% disagreed.

c. Overall 47% of people agreed that they would be willing to pay more council tax to help protect services and 40% disagreed, with 12% not voting.

d. Overall 65% of people agreed the council outsourcing functions where there was a sound case to do so.

e. Overall 69% of people agreed that we should increase the support available to help with access to services on line.

f. Overall 59% thought their area could get involved in delivering some services – 30% disagreed.

g. Overall 67% of people agreed that it was appropriate to transfer assets to local groups.

78 The events showed there is a clear appetite for people to engage in discussion about how public services are funded and organised, but people want an opportunity to have more in depth discussions and access to background information. This will inform the next stage of public engagement.

Appendices

79 Identified Directorate Savings for 2012/13 (Appendix A)

80 Medium Term Financial Strategy (Appendix B)

Background Papers

81 Joint Capital and Asset Management Strategy agreed by Cabinet – 16 December 2010

Herefordshire Council

SAVINGS IDENTIFIED FOR 2012-13

DIRECTORATE: Valued Services - Service Area - Functional Detail	PEOPLES Principles (see key)	2012-13 Original £'000	Revised £'000
Transition from Children to Adult Services		150	0
		150	**0**
Supporting the Vulnerable -			
Social Care	Developing/commissioning 'edge of care' services which will reduce the need for CYP to be looked after, thereby reducing the demand on agency & placement spend	250	250
		250	**250**
Improvement and Inclusion			
Complex Needs - contract price control	Improve contract prices / improve placement cost control by 5% pa	56	151
Youth Offending Team contract reduction	This is a jointly commissioned service for Herefordshire and Worcestershire. The number of young offenders has reduced. The service is subject to review..	35	35
Looked After Children placements	Improve contract prices / improve placement cost control by 5% pa	202	0
Trading, including drama/costume store and other CYPD activities	Increase revenue from trading services to schools, partners and the public	40	0
School Transport	Reductions in relation to route reviews and contract changes and charging	145	145
Youth Service	Changing the service offer as per Cabinet paper and current consultation	100	100
Targeted mental health in schools	Herefordshire bid in 2009 to be a targeted mental health in schools pilot area.	15	0

income generation			
Adult Services	Review of panel process and increased market development	2,083 0	8 2,383
	Cost Improvement Plan covering enablement; contract efficiencies and reviews. • reablement, enablement and assistive technology which provides greater emphasis on the reduction on prevention and reliance on long-term support by helping people live independently for longer • reducing residential care by supporting people to live independently • increased charges in order to remove current subsidy and move towards full cost recovery this is based on the individual's ability to pay • making better use of existing contracts and gaining better value for money from commissioned services. This includes re-procurement of existing services, gaining more alignment between needs and costs when negotiating rates with providers, and savings identified within existing contracts • creating a more vibrant market to offer greater choice and control to service users which includes transitions and carers services • Reduction in management overheads		
EHTS - regulatory services	Reduction in Regulatory Services Gross expenditure budget 5% 2011/12, 10% 2012/13	278	141
	Reduced subsidy via increased charges (2% @ 1.4.11)		50
	Inflationary increase on non-salary related budget	0	11
	Reduction in supplies and services	0	30
Improved cost control	Cutting costs stationery / copying etc	10	0
		2,964	**3,054**

Rising to the Challenge

Efficiency Savings	A combination of additional grant income and reconfiguration of the Connexions service into the new targeted support services team, additional target for transport route reviews and various other funding reductions.	0	480

Regulatory Services	As part of the review of regulatory services an overall savings will be made. This is the amount for 2012.13	0	200
Children & Young Peoples restructure	CYP restructure has twofold focus - to redesign services to provide efficient service model to meet requirements of locality working & to reduce staffing costs to meet financial challenges	0	340
Children's centres - management reduction	As the vision for the future delivery of children's centres develops the centres will have to be reconfigured to reduce costs, and meet national expectations. Children's centre services continue to evolve and develop and central costs have already been reduced by removing children centre specific strategic management in the current restructure. 2011/12 increased responsibility will be given to children's centre managers to develop the services - including those which can be traded, but in 2012/13 management costs will need to be reduced	100	0
		100	**1,020**

Local Delivery -

Locality Development	Move to locality teams and the co - location hubs will achieve savings in both staff time and mileage costs. Initial work has scoped a number of staff weekly movements - city based as now and in future in the hubs. The work has identified the potential for significant staff savings although at this stage are estimates.	20	0
		20	**0**

Personal Responsibility - self reliance, people and communities helping themselves, behavioural change

Daycare charging	Learning Disabilities. – removing subsidies and charging full costs	150	
		150	**0**

SUMMARY		**3,500**	**4,324**

REVIEW OF SAVINGS IDENTIFIED FOR 2012-13

DIRECTORATE: CORPORATE

Cutting Red Tape -

Service Area - Functional Detail	Principles (see key)	2012-13 ORIGINAL £'000	REVISED £'000
Directorate Savings	Next phase of Organisational Design - further reduction of management overhead (number of posts still to be decided)	345	302
		345	**302**

Cutting Costs -

DIRECTORATE WIDE	Efficiency in maintaining non pay costs at 11/12 budget levels	0	150
Additional Income	Increased income from legal services	0	33
Inflation adjustment	Review of inflation requirement for budgets	0	200
Legal	Building capacity to deliver to partners in the Health Sector, in sourcing and delivering to new clients in the local community third sector at competitive rates	90	30
Communications	Streamlining the business - securing ongoing PCT contribution for communications function, rationalising communications spend, delivering services to new clients, cutting expenditure on publications. No negative impact on service.	5	5
Human Resource (HC)	Savings will be made through economies of scale and efficiencies in shared services	173	173
Finance	The delivery of the shared service initiative will deliver back office savings, whilst ensuring front office services are protected.	166	166
Payroll & Expenses	Reduction as part of the Shared Services initiative	24	24
Estates	The OD principles will streamline the Estates structure to reduce non front line costs	98	98

Internal Audit	Outsourcing of Internal Audit in 2011 will produce additional savings	25	25
Revenue & Benefits	The transfer to Hoople will deliver savings in line with original proposed.	25	25
Creditors	The delivery of the shared service initiative will deliver back office savings, whilst ensuring front office services are protected.	0	25
		846	**954**

SUMMARY		**1,191**	**1,256**

SAVINGS IDENTIFIED FOR 2012-13

DIRECTORATE: PLACES

Valued Services - Service Area - Functional Detail	Principles (see key)	ORIGINAL £'000	REVISED £'000
Bereavement Services charging review	Impact of Charging Policy, 5% increase in both years	30	30
Markets & Fairs - charging review	Impact of Charging Policy, 5% increase in both years	16	16
Pre Application Support for Planning	Charging for Pre Application Support		
Countryside - introduce parking charges at Queenswood	New revenue opportunity would help to reduce the overall cost to the Council of countryside service provision. This would result in cutting costs and also enable the service to focus on delivery of the core business of providing a high quality countryside asset.	50	0
Review of Directorate Income Charging	Identify additional revenue streams and implement full cost recovery in line with Income Charging Policy	138	125
Review of Directorate Income Charging - Arts	Increase charge for Contemporary Craft Fair (November)	0	8
Review of Directorate Income Charging - Waste	Increase bulk waste collection fee from £15 to £20	0	5
Review of Directorate Income Charging - Transport	Increase railcard charge by £2	0	5
		234	**189**

Cutting Red Tape - less regulation and bureaucracy, smaller local government

Strategic Housing Efficiency Savings	Disinvestment in non essential commissioned services, reduction in expenditure and identified income generation	25	10
Commissioning of Car park Services & Community Protection	Review of opportunities for alternative delivery models to streamline service delivery, reduce costs and increase revenue	100	100
Partnership development - Transport (AMPS & Fleet)	Opportunity to explore efficiencies and removal of duplication through working with Strategic Service Delivery Partner indentified following review of shared services business case.	100	100
		225	**210**

Cutting Costs -

Additional Income	Car Parking charges as part of the overall strategy	0	200
Inflation adjustment	Review of inflation requirements for budgets	0	54
Efficiencies	Contract savings (£500k), Cultural Services review (£100k) and Bring Site Collections (£15k)	0	615
Contact	Supporting People review of overall funding against the £4.471m total funding envelope	0	100
Cease issuing black sacks for household waste	To be negotiated with contractor	0	200
Staff Travel Plan - introduce staff parking charges	Reduced cost of service delivery due to removal of concession and resulting increased revenue to support local priorities of economic growth through ensuring car parking priorities for shoppers	35	0
Homelessness Prevention Fund - Service review	Service Efficiency review to demonstrate value for money	20	28
Further Reduction in Staff Establishment	Phase 2 of restructure (to be finalised)	58	18

Arts & Leisure - reduction in management fee through Commissioning Agreement for Halo & Courtyard	Cost saving to council/ reduction in front line service	137	137
Reduction in contribution to Hereford Futures team	Cost saving to council	17	36
Regeneration Scheme	Regeneration in Herefordshire	133	0
		400	**1,388**

Local Delivery -

Shop Mobility Re-design	Support for shop mobility varies across the county and redesign of the service should support the desire from local areas	15	15
Community Regeneration - reduction in voluntary sector grants to Herefordshire Voluntary Action, Citizens Advice Bureau, Ledbury Voluntary Action, Voluntary Community First.	Potential Savings anticipated from 3rd Sector Review	18	18
Review of community facilities'		100	200
Cultural Services Review	Establish a Cultural Service s Review	100	150
		233	**383**

SUMMARY	**1,092**	**2,170**

REVIEW OF SAVINGS IDENTIFIED FOR 2012-13

COUNCIL WIDE:

		ORIGINAL	REVISED
-		£'000	£'000
-			
Corporate Working	Bringing services together across the Council.		594
Corporate Working	Bringing services together across the Council. (Business Support, Policy & Performance, Research) Phase 1	240	210
Corporate Working	Bringing services together across the Council. (Business Support) Phase 2		250
Corporate Working	A review of former grant based areas affected by the government's funding reduction		500
		240	**1,554**

OVERALL SAVINGS FOR ALL DIRECTORATES

DIRECTORATE	ORIGINAL	REVISED
Corporate	**1,191**	**1,256**
Peoples	**3,500**	**4,324**
Places	**1,092**	**2,170**
Council Wide Initiatives	**240**	**1,554**
TOTAL	**6,023**	**9,304**

Working together for the people of Herefordshire

Medium Term Financial Strategy

2012/15

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Medium Term Financial Strategy 2012/15

Foreword by the Council Leader and Cabinet Member – Corporate and Education

The Medium Term Financial Strategy (MTFS) is an important document, underpinning our strategic, transformational and operational intentions for Herefordshire Public Services (HPS). The strategy will support, shape and influence the challenging financial environment that public services are facing. The total resource envelope for Herefordshire Public Services is circa £650m. Our strategy is one that will need to enable a culture to develop and is one where there is a movement away from short-term budget setting to an approach that reviews all expenditure and focuses on what matters to the people of Herefordshire. 2012/13 provides a great opportunity to develop service flexibility across public services and this MTFS identifies the transfer of funding between the PCT and Council. We aim for a culture where there is less bureaucracy and where resources can be targeted towards frontline services, a culture where we stop doing things we do not need to do, ensuring a longer-term approach that brings service and financial stability to our service delivery.

The Comprehensive Spending Review (CSR) will have a significant impact on funding from central government. Throughout the coming year we will undertake a root and branch review of services, and consider alternative ways of working, in particular investigating broader partnership arrangements, to mitigate the effects.

The MTFS identifies the scale of the impact of the economic downturn that has affected the world economy and reflects this impact on Herefordshire. However, Herefordshire Council and the PCT as Herefordshire Public Services have been actively planning for the impact of the reduced settlement as part of CSR 10. A number of assumptions about cross cutting service areas that are delivered across both organisations and by working in partnership and in line with government policy will enable improved service delivery. In line with the equality act of 2010 Herefordshire Council and the PCT will ensure that any efficiency savings and service reviews will demonstrate that all financial decisions are made in a fair, transparent and accountable way, considering the needs and rights of different members of our communities. In line with government policy we will be implementing Shared Services to deliver back office savings which will be released for front line service delivery.

2012 will be both challenging and exciting as a result of not only the economic downturn but the further development of HPS to include the Herefordshire Health Care Commissioners, who now operate as a subcommittee of the PCT Board with a defined scheme of delegation.

During 2012/13 it will be more important than ever that we continue to strengthen the partnership between the council, health service providers and other stakeholders in Herefordshire. The level of service transformation, improvement in quality and ensuring services deliver value for money can only be delivered through the strength of maximising the interfaces between primary and secondary care, between health and social care and between empowered service users. This deep partnership has already demonstrated both qualitative and quantitative benefits for Herefordshire in recent years, including the Shared Services partnership, Hoople, in April 2011. However as we move forward, there will be even stronger evidence of the impact of the deep partnership. The Commissioning of integrated care pathways will deliver the service transformation that our population expects and will maintain financial stability across public services within Herefordshire.

As part of the administration's priority to deliver key projects that support economic prosperity the document includes funding envelopes for key capital projects such as the link road in Hereford for which we already have planning permission.

Cllr. John Jarvis
Leader of the Council

Cllr Phillip Price
Cabinet Member – Corporate and Education

Medium Term Financial Strategy 2012 to 2015

Foreword by the Chief Executive and Chief Officer: Financial and Commercial Services

The MTFS has helped change Herefordshire's financial management culture; it includes a requirement that responsibility for managing individual budgets rests with our budget managers who operate within our financial policies and procedures. The MTFS helps explain the overall position, so that we all know that financial management is part of our day-to-day activity and that we must demonstrate we provide value for money at a time when the economic downturn is having a widespread effect.

Herefordshire not only faces economic challenges but the demands of an ageing population will require us to transform our services to ensure that people can maintain levels of independence. HPS will need to ensure that packages of care and support do not only contribute to independence but also prevention. It is accepted that service delivery will need to be undertaken in a less institutional setting in order that the additional challenge on the service delivery agenda can be met

Planning the use of public money and transparent accountability for Herefordshire is a key priority, from which we continue to ensure Herefordshire has financial stability and also deploy resources to support agreed priorities. This cannot be achieved if we limit our planning horizon to a single year. The MTFS helps planning over a longer time framework and demonstrates how we will use our resources in the future.

The MTFS forms part of the service planning process and sets a framework for the interpretation of the council's and Herefordshire Public Services' priorities and principles, supporting and driving delivery of the next stage of the Herefordshire transformational agenda. It is an appropriate way to plan our expenditure and has played a part in helping maintain an unqualified value for money conclusion from our external auditor. However, we continue to review and, where appropriate, improve the strategy each year.

Chris Bull
Chief Executive

David Powell
Chief Officer: Finance & Commercial Services (Council)

Contents

1. Introduction

1.1 The MTFS covers the financial years 2012/2015 and demonstrates how HPS will maintain financial stability, deliver annual efficiencies, and support investment in priority services, whilst demonstrating value for money and maintaining service quality.

1.2 The MTFS is a key part of HPS's integrated corporate, service and financial planning cycle. This cycle is designed to ensure that corporate and service plans are developed in the context of available resources and that those resources are allocated in line with corporate priorities.

1.3 The continuation of the downturn in the economy has had a direct effect on the income earned from investing balances, income collected from the provision of services and increased service pressures.

1.4 In 2010 the coalition government published a Comprehensive Spending Review for 4 years 2011/12 to 2014/15 and a two year local government financial settlement. The settlement reduces public sector funding, thus providing a challenge to deliver front line services against severe financial constraints.

1.5 In December 2011 the Government announced the second year of the 2 year settlement (2012/13), which confirms further cuts for local government. The Government's Autumn Statement proposes that cuts will continue until at least 2017.

1.6 The position for 2013 onwards is less certain. The Government is introducing major changes in the way local authorities are funded and also to housing and council tax benefits. This will be monitored closely over the coming months.

2. Economic and Demand Background

2.1 Economic Growth

2.1.1 At the beginning of 2011 there was a general belief that the worst of the economic crisis was over. Whilst a long and slow recovery was anticipated, it was forecast that the UK economy would grow by around 2% in both 2011 and 2012. Demand was expected to have recovered sufficiently to enable the Monetary Policy Committee to increase the bank base rate to 0.75% in September 2011, reaching 3.00% by September 2013.

2.1.2 However, high inflation, modest pay rises, job cuts and weak consumer confidence has led to reduced demand and downward revision to growth forecasts. UK economic growth is now expected to be around 1% for 2011 and remain at this subdued level for 2012. As for the first increase in the bank base rate, some forecasts are now pushing this back to 2015.

2.1.3 The outlook for UK growth is hampered by the financial position in the Eurozone as European nations face anaemic growth, excessive debt and a lack of confidence in the ability of certain nations to honour their commitments. UK output is expected to take until 2013 to regain the ground lost since it peaked in early 2008.

2.1.4 The average of various independent forecasts gives the following medium-term projections.

	Independent average				
	2011	**2012**	**2013**	**2014**	**2015**
GDP Growth	1.0%	1.1%	2.1%	2.3%	2.4%
Inflation rate:					
• **CPI**	4.5%	2.7%	2.0%	2.2%	2.3%
• **RPI**	5.3%	3.3%	2.6%	3.2%	3.6%
Claimant unemployment	1.55m	1.75m	1.76m	1.66m	1.52m

2.2 Inflation

2.2.1 CPI inflation was 4% in January 2011 and it did not fall below 4% all year, reaching a high point of 5.2% in September before falling back slightly to 5.0% in October and 4.8% in November.

2.2.2 Inflation is expected to be lower in 2012 as the January 2011 VAT increase and past energy price hikes fall out of the statistical comparison.

2.2.3 Forecast inflation figures are shown in the above table.

2.3 Economic Summary of Herefordshire

2.3.1 The State of Herefordshire Report 2011 contains information that describes the county. Some of the key findings are:

- The population of Herefordshire is increasing due to net in-migration, although growth has slowed during the recession. Herefordshire's resident population grew by 3% between 2001 and 2010, which is the same as that of the West Midlands region overall, but lower than England and Wales (6%).

- Herefordshire's economic output is low compared to regionally and nationally and the gap has widened over the last ten years. This is a result of the lower wages and type of work carried out in the county.

- The age profile of the potential resident workforce is changing due to the aging population structure. The number of people aged 16-64 in Herefordshire has been falling since 2008 and could fall to 104,000 by 2026 (109,900 in 2008).

- The rate of self-employment is higher in Herefordshire than in the West Midlands and England as a whole and the overall employment rate in relatively high. Total unemployment, although comparatively low, is decreasing slowly and remains much higher than prior to the recession. Based on past trends total employment in Herefordshire is projected to decrease.

- Pockets of deprivation are concentrated in urban areas of Herefordshire, but smaller pockets also occur in more rural areas.

- Access to broadband, mobile phone services and other infrastructure is an issue for some residents and businesses in rural areas.

- Businesses and residents identify congestion in Hereford City as in need of improvement.

- There is a high demand for affordable properties in Herefordshire, particularly in Hereford City.

2.4 Potential Growth and Changes that will affect Service Need

2.4.1 Adult Social Care faces significant future pressures due to increased life expectancy and future demand due to an aging population

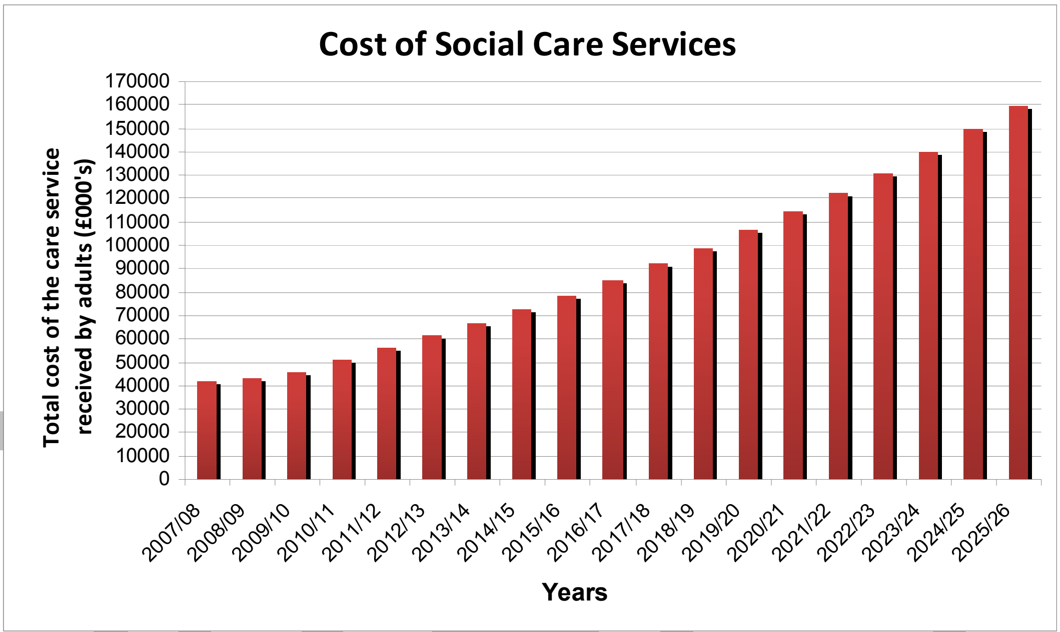
2.4.2 Over a fifth (22%) of Herefordshire's population is aged 65 and over (39,800 people), compared to 17% both regionally and nationally. In Herefordshire the number of people over 65 is expected to rise by 18% in the next five years and there are expected to be over 60,000 people aged 65+ living in Herefordshire by 2026, over 50% more than currently.

2.4.3 In particular, the number of people aged 85 and over is expected to continue growing at an increasing rate, from 5,600 in 2010 to more than 10,000 by 2026. This group makes by far the greatest demands on health and social care and is at greatest risk of isolation due to living alone and in poor housing.

2.4.4 The rate of physical disability and mental health ill health among the adult population under 65 is predicted to remain virtually the same. (Stable prevalence, no population growth until 2030). However, there is an increasing complexity of need.

2.4.5 The rate of learning disability will increase slightly in numbers until 2030. However, within this the population of clients, their carers will age significantly and younger clients joining the cohort have more intense needs. In addition their carers have more expectations for independent living.

2.4.6 The graph below illustrates the potential growth in spending on social care services based on previous years' trends and including assumptions of 2% inflation and 3% increased need due to aging population (based on last 5 years). It does not include any allowance for further changes to levels of need.



2.4.7 Numbers of children in Herefordshire are decreasing, although there have been more births than expected in recent years. The current proportion of Herefordshire's population aged under 16 (17%) is similar to England & Wales (19%), but numbers have fallen from 34,000 in 2001 to 30,800 in 2010. This decline is expected to continue and then stabilise at around 29,000 from 2016 (6% below 2010 levels)

2.4.8 Based on September 2011 pupil numbers, Primary school numbers (including nursery classes) are predicted to increase in 2012/13 by 39 pupils or 0.3%. Secondary school numbers are predicted to fall by 156 pupils or 1.6%. Since the establishment of Herefordshire Council in 1998, primary school numbers have fallen by 2,185 from a high of 14,230 in 1998, a reduction equivalent to 13.3%. From a high point in January 2005, secondary numbers have fallen from 10,511 to 9,635, a reduction of 876 (equivalent to 8.3%) and are expected to continue to fall until 2017. School Funding is based upon pupil numbers in January each year and these estimates will be updated when final pupil numbers are confirmed in late February 2012.

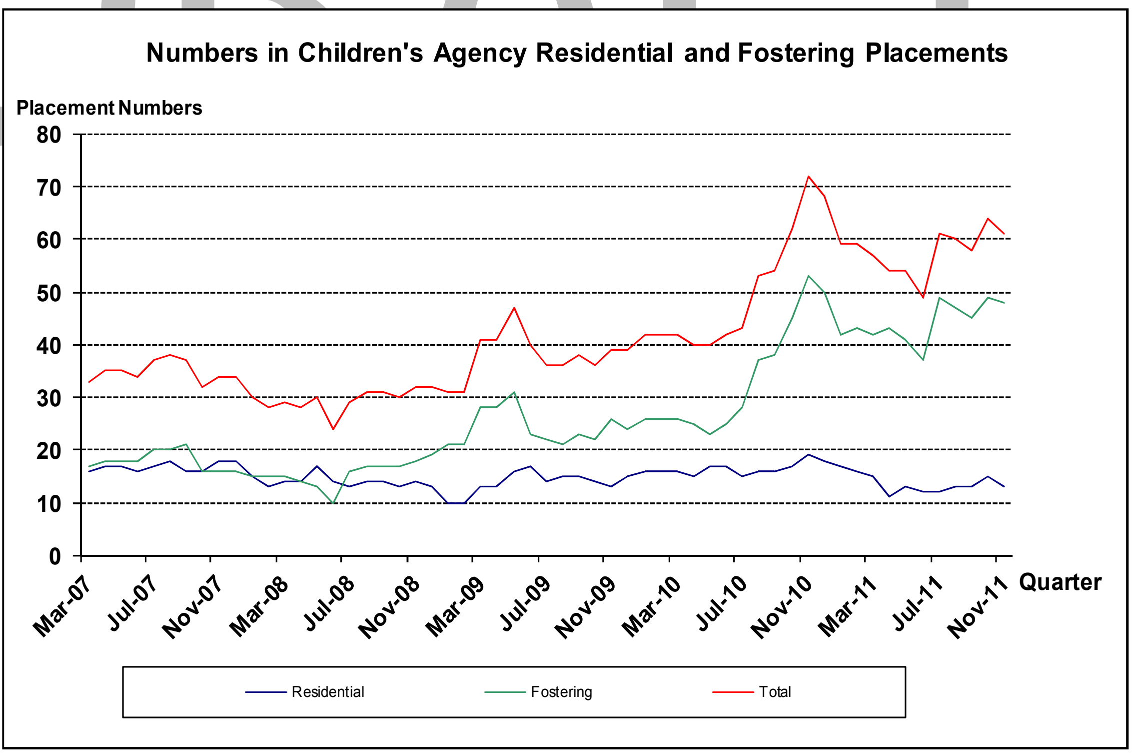
2.4.9 There has been a dramatic increase in numbers of migrant workers coming into Herefordshire, although it is not possible to determine how many have stayed or how many are in the county at any one time. Current evidence suggests that the majority of Herefordshire's migrant workers are seasonal workers and intend to stay in the UK for under a year. Although they are not counted as part of the resident population there is still an impact on services e.g. health services.

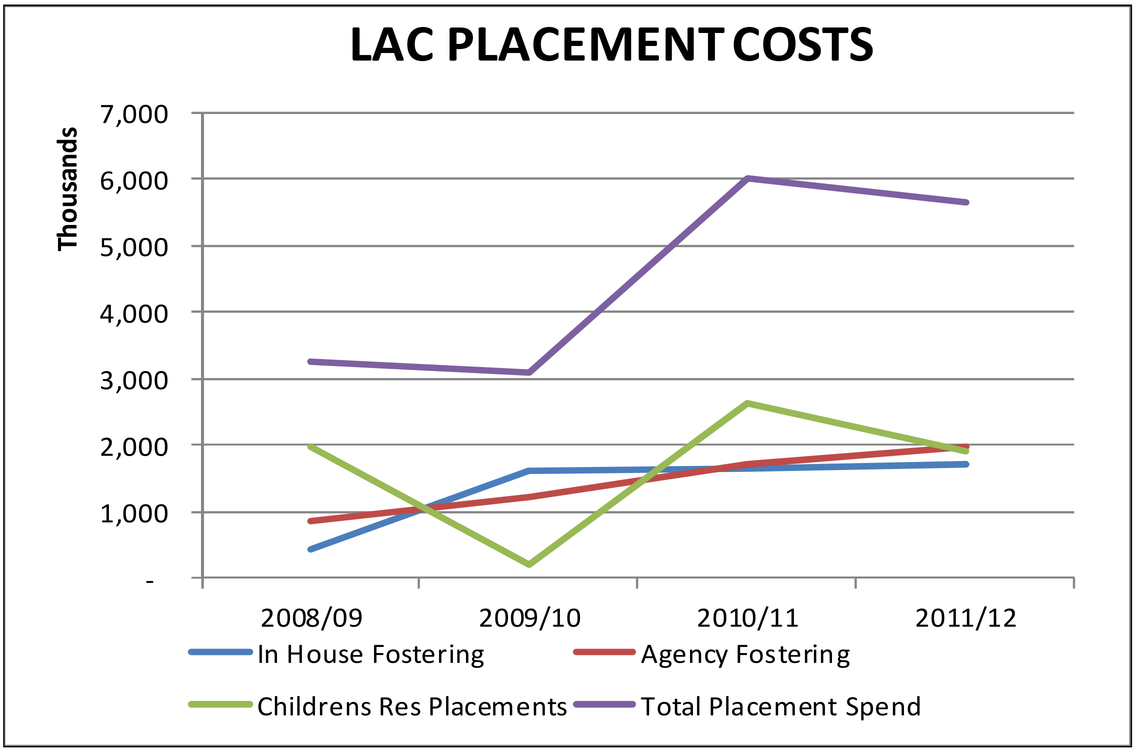
2.4.10 Historically Herefordshire has produced more waste per household and has recycled less than compared to England as a whole. However, the situation is improving to the way waste, particularly recycling, is collected. The amount that households recycle is also improving, but it is just below target. In 2010/11 households recycled on average 40% of their waste compared to 35% in 2009/10.

2.4.11 Significant challenges lie ahead in meeting landfill diversion requirements which will require significant investment in waste treatment infrastructure.

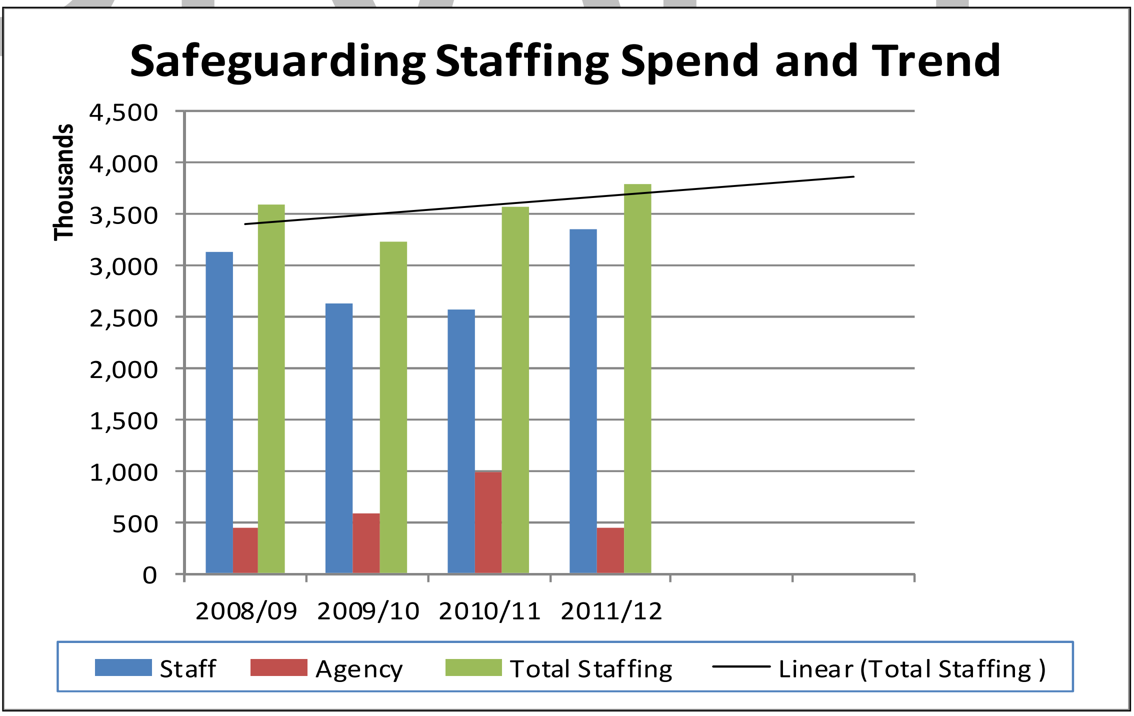
2.4.12 The impact of the 'Baby Peter' case has resulted in an increase in the numbers of children with Child Protection Plans or who become looked after by the local authority. Although there are peaks and troughs the trends for Looked after Children (LAC) continue to be upwards with a peak number in agency fostering and residential placements of 72 children in November 2010. The numbers then fell but rose again through the summer of 2011 reaching 64 in October 2011. Numbers are now falling again as efforts are made to transfer children to in house foster care or return home where it is safe to do so.

2.4.13 The Edge of Care project has been working successfully with children presented to the LAC panel to be placed in care to avoid this outcome. To date 282 weeks of care costs across 15 children have been avoided saving £133k of additional cost. The service is working actively to reduce the numbers of children in high cost placements through a combination of developing additional in house fostering capacity, edge of care intervention and the use of other carers such as special guardians or kinship carers. The tables show the growth in numbers and the increase in cost (including in house foster placements)





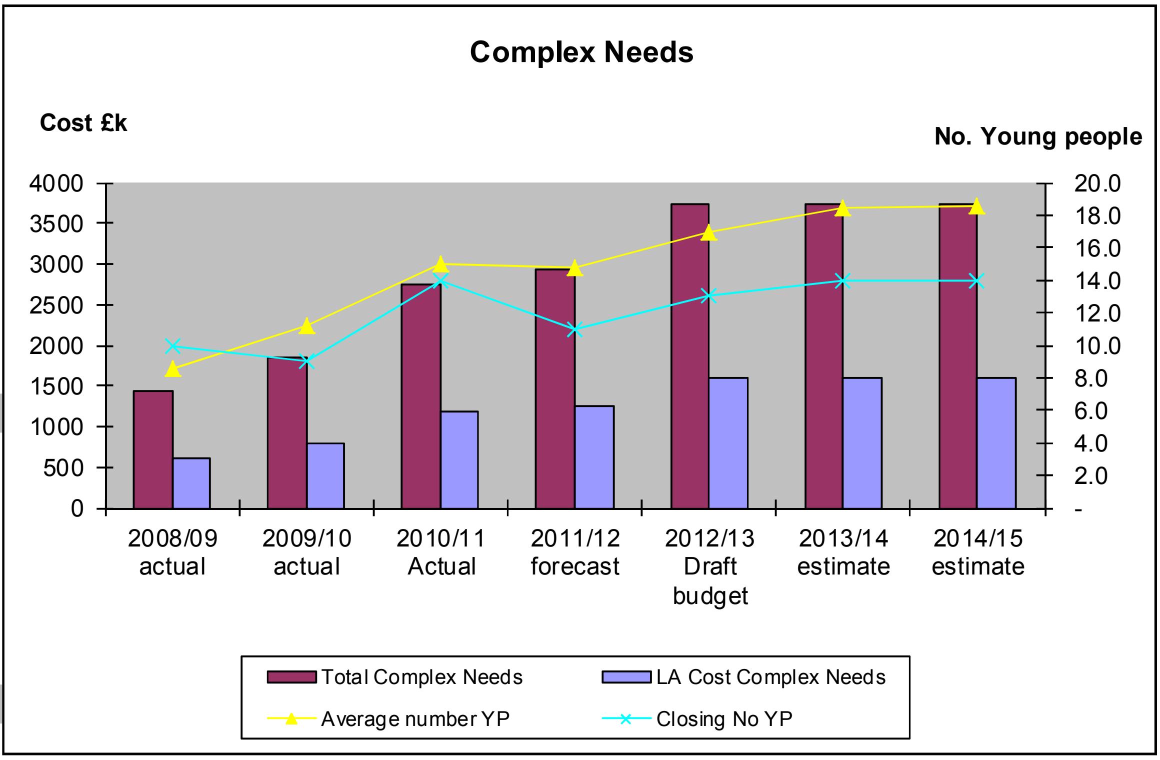
2.4.14 The increasing number of children requiring protection or care has placed additional pressures on the Safeguarding staffing budget. The on-going shortage of qualified and experienced social workers has resulted in a need to rely on high cost agency staff to ensure that appropriate case-loads for social workers are maintained. The patterns and trends are represented graphically below:



2.4.15 Within Complex Needs there have been some cases which have either moved out of Herefordshire or moved to children's or adult's social care with the result that the service is expected to make savings in 2011/12 compared to the budget.

However there have still been 3 new cases accepted in year and this trend is expected to continue. Due to the age profile of the children only 1 child in each of 2012/13 and 2013/14 will reach the age to transfer to adult social care so the budget is projected to stay at a similar level for the next three years, but this can change with a single high cost placement.

2.4.16 Of particular concern is average cost per placement which, based upon current cost will rise from £165k per annum in 2011/12 to £185k per annum in 2012/13 due to increasing complexity of cases and rising costs of placements.



3. Herefordshire's Policy Context

3.1 Introduction

3.1.1 This section of the MTFS describes the local policy context for Herefordshire.

3.2 Herefordshire Sustainable Community Strategy

3.2.1 *The Herefordshire Sustainable Community Strategy 2006 to 2020* sets out what the council and its partners aim to achieve to make the county an even better place to live and work. The strategy is being reviewed for 2012 to focus even more on the people and places of Herefordshire.

3.3 Corporate Plan

3.3.1 The council, working with NHSH, have a joint corporate plan that sets out the vision for Herefordshire Public Services 2012-15 including how the aims and objectives of the *Herefordshire Sustainable Community Strategy (HSCS)* will be realised. The vision is 'Working together to deliver efficient excellent services and improve outcomes for the people of Herefordshire'.

3.3.2 The Joint Corporate Plan contains the current overall targets, milestones and actions, together with the current budgets and other resources to achieve them, over the coming years.

3.3.3 The shared values expressed in the Joint Corporate Plan themes are:

- People – treating people fairly, with compassion, respect and dignity,
- Excellence – striving for excellence and the highest quality of service, care and life in Herefordshire,
- Openness – being open, transparent and accountable for the decisions we make,
- Partnership – working together in partnership and with all our diverse communities,
- Listening – actively listening to, understanding and taking into account people's views and needs,
- Environment – protecting and promoting our outstanding natural environment and heritage for the benefit of all.

3.3.4 The priorities of the joint Corporate Plan are:

- Create a thriving economy
- Improve Health Care & Social Care
- Raise standards for Children and Young people
- Promote self-reliant local communities
- Create a resilient Herefordshire
- Commission the right services

3.4 Corporate Financial Objectives

3.4.1 Herefordshire's financial management objectives are to:

a) Ensure budget service plans are realistic, with balanced budgets and support corporate priorities.

b) Manage spending within budgets; Directorates have a 'non-negotiable' pact to manage outturn expenditure for each financial year within budget.

c) Ensure sustainable balances, reserves and provisions, within a reasonable limit, consistent with the corporate financial risks and without tying up public resources unnecessarily.

d) Create the financial capacity for strategic priorities for service improvement.

e) Support a level of capital investment to meet the council's strategic requirements.

f) Maintain a strong balance sheet position.

g) Deliver and capture year on year efficiency and Value for Money improvements.

h) Ensure an integrated approach to corporate, service and financial planning in full consultation with key stakeholders.

i) Ensure a whole-life costing approach is taken to both revenue and capital spending decisions.

3.5 Working in Partnership

3.5.1 Herefordshire welcomes the opportunity to work with strategic partners to improve outcomes. However, to achieve its corporate financial management objectives, we will always seek to ensure:

a) The financial viability of partners before committing to an agreement.

b) Clarity of respective responsibilities and liabilities.

c) Accounting arrangements are established in advance of operation.

d) Implications of terms and conditions on any associated funding are considered in advance of operation

3.5.2 From April 2011 an Integrated Care Organisation for Herefordshire was established, Wye Valley NHS Trust, comprising the provider arm of the council and NHSH, alongside Hereford Hospital Trust. The aim is delivering health and social care which is focused on providing care as close as possible to people's homes, rather than in an institutional setting; a model which is also aimed at identifying our most vulnerable citizens and shifting the emphasis from diagnosis and treatment to prediction and prevention. The creation of the Wye Valley Trust will deliver financial savings across the health sector which will contribute towards financial viability.

3.5.3 Mental health services are being delivered through an established specialist trust (2gether) in order to deliver and modernise services, using the care professionals transferring from the existing organisations.

3.5.4 Back office functions are provided through a joint-venture company, Hoople, established in April 2111. Savings targets for council support have been agreed amounting to £467k in 2011/12, £413k in 2012/13 and £340k in 2013/14.

3.6 Managing External Funding

3.6.1 Grants provide another opportunity to increase financial capacity. The MTFS will be to pursue such opportunities, providing that:

a) Match funding requirements are considered in advance.

b) They support, or do not conflict or distract from, corporate priorities.

c) They have no on-going commitment that cannot be met by base budget savings.

d) They do not put undue pressure on existing resources.

e) The net cost overall is not excessive

3.6.2 ***Managing Developer Contributions*** - This is another source of external funding that can be secured through the planning system. It may be possible to secure funding to support the cost of day-to-day services (e.g. commuted sums for maintenance of public open spaces). Support for capital infrastructure can also be achieved in this way (e.g. developer contributing to cost of new access roads). HPS aims to maximise the potential for increasing financial capacity and managing growth in volumes through s106 agreements, where possible. The council is in the early stages of producing an action plan for the implementation of a Community Infrastructure Charging Levy. It is envisaged that the CIL will be adopted in Spring 2013.

3.6.3 ***Managing Fees and Charges*** - The council has developed a charging protocol with the aim of implementing a corporate charging policy. The policy will recognise the potential for discretionary charges to fund services and ensure full cost recovery where feasible and minimise the subsidy from council budgets.

3.7 Governance

3.7.1 Maintaining strong financial control is a prerequisite to achieving the council's corporate priorities and the integrity of the MTFS. Good systems and procedures are in place for regularly reporting on financial performance to Cabinet, as part of the integrated performance framework.

3.8 Value for Money and Efficiency

3.8.1 Herefordshire's strategy for securing efficiency gains is to seek continual improvement in the productivity of all our resources, including people, land, property, ICT and cash.

3.8.2 Herefordshire Council and PCT have a joint Value For Money Strategy. This has built on the development of the routine use of VFM information and benchmarking data to review and challenge VfM throughout services and corporately, supporting continuous service improvement and the drive for efficiencies

3.8.3 We support the drive for VfM through the following mechanisms:

- Ensuring service managers deliver the outputs and outcomes agreed for their service area within budget; managing within budget is a key responsibility for all budget holders embedded in our staff review and development procedures.
- Support from Procurement through efficient tender and other procurement processes that ensure robust quality and price.
- Integrating corporate, service and financial planning processes.
- Planning over the medium-term as well as the short-term.
- Benchmarking our costs and activities, year on year and with other authorities.
- Through internal and external audit reviews.

3.9 Root and Branch Reviews

3.9.1 A programme of root and branch reviews will be undertaken over the medium-term to address the council's funding challenge. The key features are likely to be;

- Ensuring we focus on the priorities for our residents and Herefordshire
- Reshaping service for the future, working with others
- Improving quality and performance
- Reducing our costs still further, providing value for money
- Consultation and engagement with employees, service users and partners

4. National Financial Context

4.1 Introduction

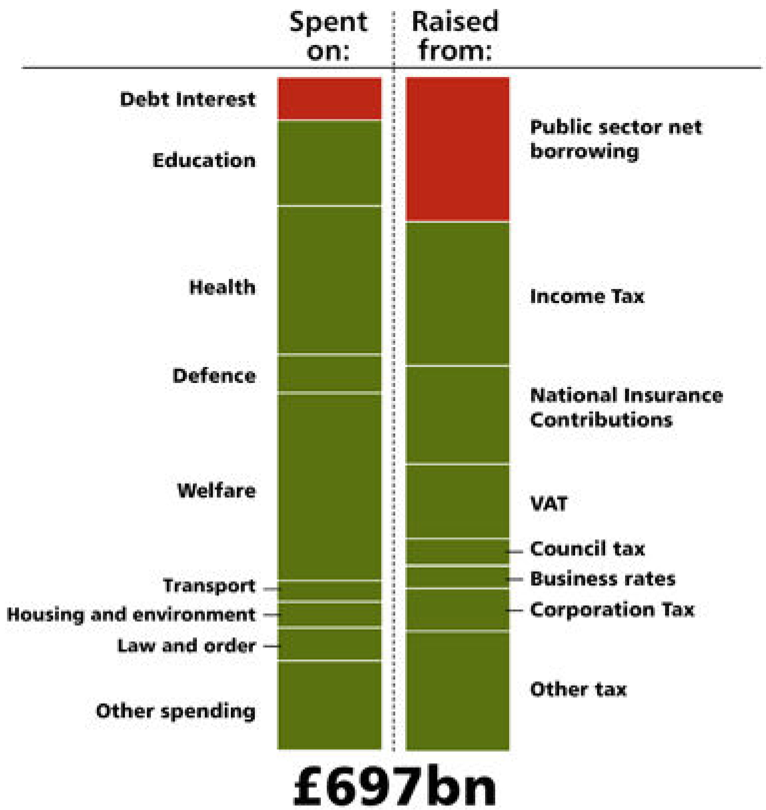
4.1.1 This section of the MTFS sets out the financial context at national level across both NHSH and Herefordshire Council. Central government's plans for public spending is documented in the following sections.

4.2. Four Year Spending Review

4.2.1 On 22nd June 2010 the Coalition Budget gave the overall level of public spending for the four years from 2011/12 to 2014/15 (spending envelope). The Comprehensive Spending Review 2010, announced on 20th October 2010, was the process through which this spending envelope was allocated to pay for all areas of government activity including public services, social security, and administration costs.

4.2.2 The Government was borrowing one pound in every four that it spent and the UK was spending £43 billion on debt interest, which is more than it spent on schools in England.

4.2.3 The diagram below shows government spending on debt interest and amount of borrowing as part of the total budget:



4.2.4 The Government said that tackling Britain's deficit was its top priority and that it was necessary to secure sustainable economic growth. The consequences of not acting could be serious: higher interest rates, business failures and rising unemployment.

4.2.5 The Spending Review set out spending plans for the four years until 2014/15. In its approach to these choices, the Government prioritised:

- spending that promotes long-term growth, and creating the conditions for a private sector-led recovery and
- fairness, with all sections of society contributing to tacking the deficit, whilst protecting the most vulnerable and providing opportunity for the poorest.

4.2.6 This was underpinned by a radical programme of public service reform, improving transparency and accountability, giving more power and responsibility to citizens and enabling sustainable long term improvements in services. It also included further savings and reforms to welfare, environmental levies and public service pensions. Around 490,000 public sector jobs were estimated to be lost over the period and on average departmental budgets will be cut by 19% over the four-year period.

4.2.7 The Spending Review also delivered the Government's specific commitments set out in the Coalition Agreement to:

- increase NHS spending in real terms in each year of this Parliament;
- spend 0.7 per cent of Gross National Income on overseas aid by 2013 and
- restore the earnings link for the basic state pension from 2011, as part of the triple guarantee of using earnings, prices or 2.5 per cent, whichever is highest, from April 2011

4.2.8 The main changes for local government announced in the 2010 Spending Review were:

Formula Grant

- Formula Grant decreased on average by 9.9% in 2011/12
- From April 2011 grants currently paid outside Formula Grant worth more than £4bn, were rolled into Formula Grant.
- An additional £1bn for personal social services was to be included in Formula Grant by 2014/15.

Un ring fencing Grants

- From April 2011 onwards, grant streams to local authorities were reduced to less than ten.
- All ring fencing on grants was removed, except from the Dedicated Schools Grant and a new grant for public health, to be introduced in 2013.
- A separate new unringfenced Early Intervention Grant, worth around £2bn was introduced.

Council Tax Freeze

- Authorities, which chose to freeze Council Tax in 2011/12, had 'the resultant loss to their tax base funded at a rate of 2.5% in each year of the Spending Review period'.

Social Care

- £1bn will be put into Formula Grant for Personal Social Services, meaning total funding for social care, including rolled-in grants, will be £2.4bn a year by 2014/15.
- In addition, £1bn of funding will be provided through the NHS budget to support joint working between the NHS and councils in the provision of social care.

Transport
- Bus Operators' Subsidy was reduced by 20%, saving over £300m by 2014/15.
- Statutory concessionary travel entitlements remained.
- Revenue grants to local authorities from DfT were reduced by 28%.
- The number of transport grants to councils reduced, with greater control and flexibility over spending these grants.

Education
- The schools budget for 5 to 16 year olds to increase by 0.1% in real terms each year of the Spending Review period. This included £2.5bn of funding for the new pupil premium.
- £15.8bn of capital funding would be made available for schools over the Spending Review period. The Government would rebuild or refurbish over 600 schools from the Building Schools for the Future and Academies programme.

Housing
- The 'New Homes Bonus' was introduced to incentivise councils to grant planning permission for the construction of new homes, by matching council tax receipts for each new home built or vacant property brought back into use, for a number of years. In addition £350 will be given for every affordable home provided.

Economic Growth
- The Regional Growth Fund was announced, to be worth over £1.4bn over three years. It is designed to help areas most dependent on public sector employment to make the transition to private sector growth. Both private bodies and public-private partnerships will be able to bid for the funding by demonstrating that their proposal will bring in private investment and support sustainable increases in private sector jobs and growth in their area. Bids are likely to exceed £1m, have significant private sector leverage, contribute towards green growth and integrate with planning policy. A panel will assess funding bids from Local Enterprise Partnerships as well as the private sector.

Council Tax Benefit
- From 2013/14 Council Tax Benefit will be localised; Government also plans to reduce spending by 10%.
- Government will consider measures to give authorities more flexibility 'to manage pressures on council tax', to be implemented from the same date.

Local Authority Borrowing
- Interest rates on loans from the PWLB increased to 1% above the rate for British Government gilts, previously the rate tracked gilts. The Treasury

estimated this would lead to a reduction of 17% in self-financed expenditure by councils over the Spending Review period.

Internal Restructuring

- In 2011/12 a £200m capitalisation fund was made available for capitalisation to support authorities wishing to deliver savings through internal restructuring.

4.3 Local Government Settlement 2011/12 and Provisional 2012/13

4.3.1 The Provisional Local Government Finance Settlement was presented to the House of Commons on 13th December 2010, ratified in the Final Local Government Finance Report (England) presented in a written statement to the House of Commons in February 2011.

4.3.2 A key message contained in the settlement was that local government has been given flexibility to take decisions locally to address local priorities. Restrictions were lifted on how local government spends its money by removing "ring fences". The intention was to give councils extra flexibility to make decisions about where savings are found. However, this is subject to the usual rules to ensure that capital funding is used on capital expenditure.

4.3.3 The settlement included the distribution of Formula Grant totals amongst local authorities for a two year period. A second two year settlement is expected to follow, for which Government intend to adopt a new distributional system.

4.3.4 A significant factor that added to the pressure faced in 2011/12 was the front loading of funding reductions. The profile of reduction is therefore uneven and for Herefordshire is 13.3%, 8.6% for the first two years (the government figures using 'like-for like comparisons).

4.3.5 The settlement confirmed the changes set out in the Spending Review including the reduction of specific grants, the council tax freeze grant, and the New Homes Bonus. The ability to capitalise redundancy costs was also confirmed. £1bn additional funding for social care is to be included within the formula grant by 2014/15. NHS Funding of £648m in 2011/12 and £622m in 2012/13 was identified to support integrated working between health and social care.

4.3.6 Other headline changes were;

- Significant formula distribution changes – concessionary fares, social care and transport.
- Damping arrangements were in place based on four banded floors and dependency on formula grant; Herefordshire in Band 3
- Those worst hit by the changes (limited to 8.8% of spending power reduction) were provided with a transitional grant of £85m
- A New Homes Bonus was introduced to incentivise the support of new housing development
- Dedicated Schools Grant had an overall increase of 1%, but this translates into a flat cash per pupil increase, due to pupil number rises. There was a minimum funding guarantee at school level of -1.5%
- Pupil premium of £625m was to be distributed, which has been set at £430 per free school meals pupil for the first year

- Pupil premium was to rise to £1,750 per free meals pupil as the premium increases over the next four years

4.3.7 The Government introduced a measure known as "local authority spending power". This is based on funding from central government (including formula grants, specific grants and NHS funding to support social care) plus council tax receipts.

4.4 Autumn Statement – November 2011

4.4.1 On 29 November 2011 the Chancellor of the Exchequer made his Autumn Statement to the House of Commons updating MPs on economic and fiscal forecasts for the UK economy. Key points for councils were;

- The Chancellor confirmed that there would be no change to the figures already announced in the 2010 Spending Review. He added that he had set new Expenditure Totals for the end of the spending review period: 2015/16 and 2016/17. Over these two years, the Total Managed Expenditure is set to fall by 0.9% a year in real terms, excluding one-off investments in infrastructure announced in the Autumn Statement.

- The Statement reiterated the Government's offer of a one-off council tax freeze grant in 2012/13 "to help with the rising cost of living", which had been announced previously

- The Chancellor announced an extra £1.2bn spending on schools. £600m will help the local authorities with the greatest basic need for schools places and is hoped to fund an additional 40,000 places. The remaining £600m will support reforms and build 100 additional Free Schools – including Maths Free Schools for 16-18 year olds. He also announced that the number of childcare places for deprived 2 year olds will double from 130,000 to 260,000.

- Following the 2-year pay freeze there will be a 1% cap on public sector pay. There will also be a review of regional pay.

- The small business rate relief holiday was extended for a further 6 months to 1 April 2013.

- 2012/13 business rates are to be up-rated in line with September RPI at 5.6%. Businesses will be given the opportunity to defer 60% of the increase to be repaid in the following 2 years.

- An extra £1bn was announced for the Regional Growth Fund over the remaining Spending Review.

4.5 Provisional Local Government Finance Settlement 2012/13

4.5.1 2012/13 provisional Formula Grant allocations were republished on the 8 December 2011 and remained unchanged from the January 2011 figures. The Final 2012/13 Settlement is expected in late January/early February.

4.5.2 The following key announcements were made in the Provisional 2012/13 Settlement:

Formula Grant

- Formula grant in total will fall by a further 7.7% on top of the 9.9% fall in 2011/12.

- A transitional grant of £20m has been allocated for 2012/13 for authorities whose revenue spending power would have fallen more than 8.8% (benefiting 12 authorities). Spending power is defined as Formula Grant plus council tax plus some specific grants.

- Damping will continue with floors announced in February 2012

Council Tax Freeze Grant

- Formula Grant figures have also been increased to include the second allocation of 2011/12 Council Tax Freeze Grant.

- There will be a grant for councils who freeze their council tax in 2012/13, which will be paid for one year early. It will be equivalent to an increase of 2.5% on council tax (for 2012/13 only).

Specific Grants

- There have been a number of announcements relating to other key local government grants. Allocations for Herefordshire are set out in paragraph 6.4.1.

- There has been an increase in the Early Intervention Grant (EIG) following the Chancellor of the Exchequer's announcement in the Autumn Statement that early education entitlement for two year olds will be expanded to cover around 260,000 children.

New Homes Bonus

- The 2010 Spending Review allocated £200m in 2011/12 and £250m per annum for the following three years of the Spending Review period. Funding beyond this amount will come from Formula Grant. However, DCLG stated that funding for the scheme in 2011/12 and 2012/13 would be fully met by the Department and no authority will lose further Formula Grant.

- Provisional 2012/13 allocations total £431m (£199m for the second year 1 instalment and £232m for the first year 2 instalment). Based on a central estimate of housing supply £176m was top-sliced from 2012/13 Formula Grant to fund the scheme in 2012/13 along with £250m under the Spending Review. Provisional 2012/13 New Homes Bonus allocations therefore exceed available funding in 2012/13. The Bonus will therefore now be paid in 13 monthly instalments commencing in March 2012 and £6m will be recouped from local government resources in 2013/14. Final allocations will be issued alongside the Local Government Finance Settlement.

Council Tax Referendum

- On 15 November 2011 the Localism Bill completed its passage through Parliament with Royal Assent. The Localism Bill made provisions to give residents the power to instigate local referendums on any local issue and the power to veto excessive council tax increases.

- The statement confirmed what the Government would deem an "excessive" council tax increase. This will be finalised with the publication of the Final 12/13 Settlement. Local authorities will be required to seek the approval of their local electorate in a referendum if, compared with 2011/12, they set council tax increases that exceed:

    - 3.5% for most principal authorities;
    - 3.75% for the City of London;
    - 4% for the Greater London Authority, police authorities, and single purpose fire and rescue authorities.
    - No equivalent principles for town and parish councils for 2012/13 are proposed, although they may in the future.

Local Government Resource Review

- It was confirmed that the Government will shortly be publishing their response to the Local Government Resource Review (LGRR) consultation, which closed on 24 October 2011 (which was subsequently published on 19th December). The Local Government Finance Bill will provide the legal framework for the Business Rates Retention proposals.

- The Review has set out proposals for a business rates retention system, giving an incentive for local authorities to promote business development in their area.

Academies

- The adjustments for Academies' funding have not changed from those previously announced However, the Department for Education, in consultation with the Secretary of State for Communities and Local Government, has been reviewing the amount and distribution of the funding transfers from local government for 2011/12 and 2012/13 to reflect the responsibilities transferring from them when schools convert to academies. No final decisions have yet been taken regarding the amount and distribution of these funding transfers.

- For 2012/13 the top-slice from Formula Grant will remain at £265m, but a new methodology will be used to calculate individual authorities' contributions. Where this methodology suggest authorities have had more taken away than they should they will receive a specific grant. There will be no adjustment where the calculation suggests that an authority should have contributed more.

Schools and Children's Services funding

The Department of Education made a separate announcement on Dedicated Schools grant and Pupil Premium;

- DSG to be same flat cash per pupil, the rate therefore remains at £4723.65 per pupil – so no increase in pupil funding for any authority

- The Minimum Funding Guarantee remains at -1.5% - as expected

- The spend on the pupil premium will double to £1.25bn. This is as expected.

- The pupil premium to be £600 per free school meals pupil and Looked After Children and £250 for service children (up £50 from £200). The basis for payment has been widened so that it includes pupils who have ever had free school meals within the last 6 years. This will widen eligibility by approximately 30% and hence depresses the payment rate per individual pupil.

5. Herefordshire Council's Financial Context

5.1 Introduction

5.1.1 This section of the MTFS describes the council's financial position. It also covers Herefordshire's financial management proposals to achieve the corporate financial objectives set out in Section 3. This section also describes the financial approach for:

- Revenue spending.
- Capital investment.
- Treasury management.

5.2 Comparative Funding Position

5.2.1 Herefordshire is not a well-resourced council. Government grant systems attempt to make allowance for the additional cost and complexity of delivering services in a sparsely populated area but do not do enough for councils like Herefordshire where its sparse population is more evenly distributed throughout the area.

5.2.2 The Rural Services Network, a body representing rural councils in England, has established that an urban area on average receives 50% central government greater assistance than a rural area.

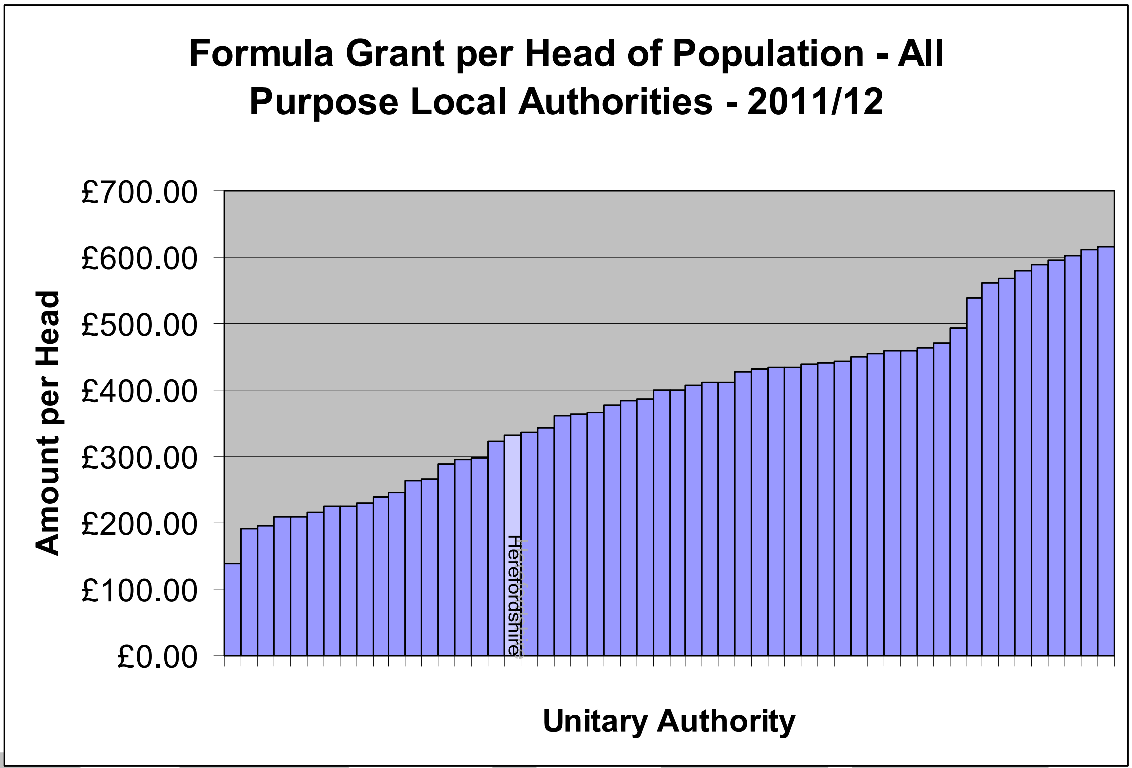
5.2.3 The 2011/12 settlement figures show that:

a) Formula Grant per head of population is £332.25 – 13% below that national average of £382.23

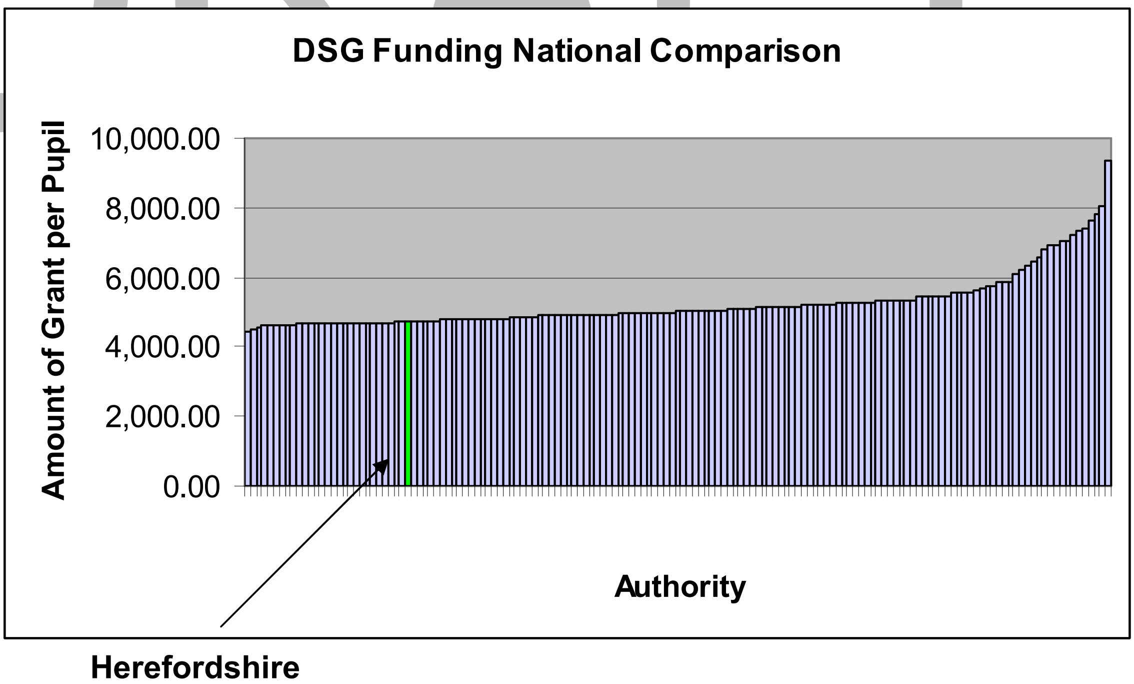
b) Indicative Dedicated Schools (DSG) Grant per pupil is £4,723.65 – 7% below the average for education authorities of £5,082.54.

c) Formula Grant plus indicative DSG per head of population is £808.10 – 18% below the unitary authority average of £984.07

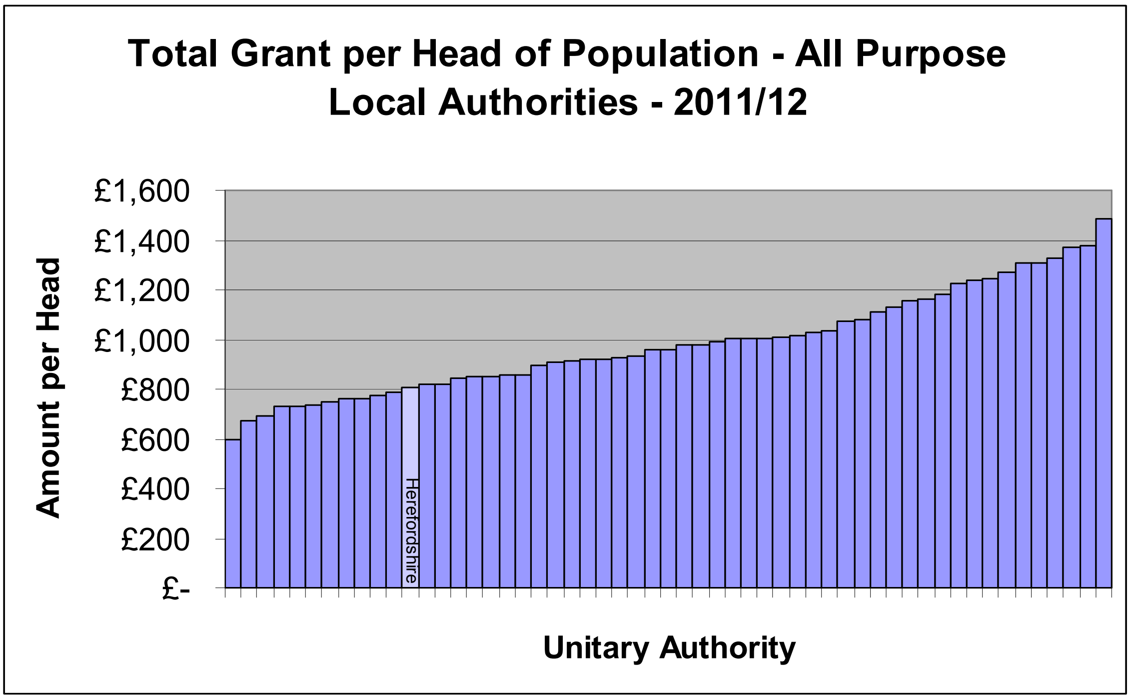
5.2.4 The graph below shows Formula Grant per head of population for all unitary authorities 2011/12. It shows that Herefordshire is 37th out of 55 unitary authorities.



5.2.5 The graph below shows DSG per pupil for local authorities providing education functions. Herefordshire is 123rd out of 151 authorities and £358.89 per pupil below the national average.



5.2.6 The final graph below shows the grant per head of population, including both the Formula Grant and the DSG for all unitary authorities for 2011/12. It shows that Herefordshire is 44th out of the 55 unitary authorities.



5.3 Formula Grant

5.3.1 The provisional local government settlement for 2012/13 was announced on 8th December 2011. The formula grant for Herefordshire remains unchanged from the figure previously announced of £54.462m, but added to that was the second year of the 2011/12 council tax freeze grant of £2.153m (£56.615m Formula grant in total). This compares to £60.191m in 2011/12 (excluding council tax freeze grant), a cash reduction of £5.7m (9.5%).

5.3.2 The government calculates an adjusted figure for 2011/12 to enable a like-for-like comparison with 2011/12, which has been calculated as £59.606m. It is estimated that this calculation has cost the council £584k, the main reason being the way that schools budgets have been transferred to academies. Herefordshire's reduction against the adjusted 2011/12 Formula Grant is £5.144m or 8.6%.

5.3.3 As in previous years there are floor-damping arrangements to limit the amount an individual council's funding reduces, which is funded by top-slicing other councils. In 2012/13 Herefordshire is losing £1.16m though floor damping, compared to a gain of £14k in 2011/12.

5.3.4 Some additional funding is provided for in the provisional 2012/13 settlement:

- £1.5m social care funding within formula grant
- £2.1m council tax freeze grant (a one-off grant, unlike the 2011/12 grant which falls out in 2015/16)
- £2.3m NHS funding to support social care, money which is held by NHSH, but will be distributed on submission of robust business cases

5.4 Specific Grants

5.4.1 The number of specific grants has reduced dramatically, with only the following allocated for 2011/12 and 2012/13 (excluding DSG and council tax grant);

List of Specific Grants	2011/12 £000	2012/13 £000
Early Intervention Grant	6,501	7,097
HCTB Admin	1,228	1,177
Music grant	263	236
Community Safety	158	80
Hone to school transport	435	540
Lead Local Flood Authorities	130	200
Learning Disability	3,657	3,738
Preventing Homelessness	225	225

5.4.1 In 2011/12 £13.5m of specific grants and Area Based Grant were moved into formula grant, but reduced to an estimated £10.8m, leaving a funding shortfall of £2.7m. A further £932k reduction in these grants is estimated to be included in the Formula Grant reduction.

5.4.2 In 2011/12 the Early Intervention Grant replaced non-ring-fenced funding from the Department for Education. Grants totalling £7.07m were transferred into the Early Invention Grant and reduced to £6.501m in 2011/12, leaving a funding shortfall of £569k. The Early Intervention Grant has increased to £7.097m in 2012/13, an increase of £596k. However, this increase comes with additional responsibilities to provide pre-school places for vulnerable 2 year olds.

5.5 Revenue Spending Power

5.5.1 In response to concerns that the grant reductions for 2011/12 and 2012/13 were front-loaded the Government focused on a council's 'spending power' rather than just Formula Grant. Spending power includes other government grants, NHS support for health and social care and council tax receipts. The Government have guaranteed that no authority will see their spending power fall by more than 8.8% in 2011/12 or 2012/13.

5.5.2 By this definition Herefordshire's spending power reduced by £5.3m (3.16%) in 2011/12 and (£4.8m) 3% in 2012/13.

5.6 New Homes Bonus

5.6.1 The New Homes Bonus commenced in April 2011, which match funds the additional council tax raised for new homes and empty properties brought back into use for the following six years.

5.6.2 Herefordshire has been awarded £591k per annum for 2011/12 (paid for 6 years from 2011/12) and provisionally £824k for 2012/13 (paid for 6 years from 2012/13).

5.6.3 The council's Financial Resource Model (FRM) assumes £800k new allocations for future years. However, the Government has indicated that from 2013/14 the funding will be top-sliced nationally from Formula Grant and therefore an element of top-slice is built into the FRM for Herefordshire.

5.7 Capitalisation Direction

5.7.1 In January 2011 local authorities were notified of the process for bidding for capitalisation directions to enable redundancy costs in 20111/12 to be capitalised and funded over more than one year. The Government had allocated £200m to be allocated after taking into account authorities' reserves. Herefordshire submitted a bid and were successful in being allocated £1.543m.

5.8 Dedicated Schools Grant

5.8.1 The Dedicated Schools Grant (DSG) is paid as a ring-fenced specific grant and used in support of the Schools Budget. It is the main source of income for schools. DSG is based upon a per pupil formula using the actual pupil numbers from the January school census data each year. Government sets a fixed amount per pupil, which is multiplied by the total pupil numbers to determine the final grant. There is specific grant certification and audit requirements to ensure appropriate use of the grant and any under or overspends must be carried forward to the next financial year.

5.8.2 National funding reflects factors such as deprivation, sparsity and area cost adjustments which affect urban and rural areas in different ways. The current grant methodology ("Spend Plus") underlying the allocation of DSG to individual authorities is determined by central government. A national review of the distribution formula for DSG based around the introduction of a national schools funding formula has commenced. Implementation is expected to be phased in over a number of years from April 2013. Further consultation papers (due in summer 2012) will set out more detail however early indications from the Institute of Fiscal Studies suggest that Herefordshire schools will lose funding in the move to a national funding formula.

5.8.3 As expected there will be no uplift in DSG for 2012/13 which will continue to be paid at the same rate as in 2011/12 i.e. £4,723.65 per pupil. DfE have not provided an overall total and expect councils to work to our own estimates. Based on the September pupil count we now estimate 22,600 pupils i.e. a loss of 117 pupils. The reduction in secondary pupils is expected to be offset by an increase in early years and primary reception children. Final pupil numbers will be confirmed in late February following the 2012 pupil census. Estimated DSG for 2012/13 is:

2012/13 Estimated Allocations	£m
DSG at 22,600 pupils x £4723.65 per pupil	106.75
TOTAL DSG 2012/13	**106.75**

5.8.4 For 2012/13 the increased spend on special educational needs and the implementation costs of the mainstreamed school grants review suggests a DSG shortfall of £0.9m, equating to £40 per pupil. There is an increase in the pupil premium to £600 for free school meals pupils and looked after children. The DfE are to widen the eligibility of the pupil premium so that pupils who have been entitled to free schools meals in the last six years will now receive pupil premium. The increase in the pupil premium is worth approximately £1m extra to Herefordshire in 2012/13.

5.8.5 Academies are publicly funded independent local schools that provide a first class free education. Academies are independent of the council and responsible directly to and funded directly by government. They are freed from national restrictions such as the teachers' pay and conditions documents, the national curriculum and Ofsted inspection requirements. Many Herefordshire schools have embraced the change and approximately 40% of pupils will be educated in Academies from April 2012.

5.8.6 Academies provide a teaching and learning environment that is in line with the best in the maintained sector and offer a broad and balanced curriculum to pupils of all abilities, focusing especially on one or more subject areas (specialisms). As well as providing the best opportunities for the most able pupils and those needing additional support, academies have a key part to play in the regeneration of disadvantaged communities.

5.8.7 Academies receive additional top-up funding to reflect their extra responsibilities which are no longer provided by the local authority.

5.8.8 Herefordshire's reduction for schools moving to academy status from formula grant was £650k in 2011/12, irrespective of the number of academies. The reduction in 2012/13 will be calculated on an amount be pupil (yet to be published) but will be subject to the maximum £500k previously announced. However there will be a rebate if the numbers of pupils transferred to academy schools results in a lesser amount. In addition there will be similar reductions on a per pupil basis to the Dedicated Schools Grant reflecting the transfer of responsibility to academy for some grant funded services. Such services will need to charge to mitigate this reduction, for example within school improvement, strategic management and property.

5.9 Council Tax

5.9.1 Authorities, which chose to freeze council tax in 2011/12, had the resultant loss to their tax base funded at a rate of 2.5%, equating to £2.1m in 2011/12, in each year of the Spending Review period'.

5.9.2 The scheme is voluntary; and applies separately to each billing and major precepting authority in England (including police and fire and rescue authorities) rather than to each council tax bill issued. Local precepting authorities, such as town and parish councils, are not included in the scheme.

5.9.3 The government has offered a council tax freeze grant for 2012/13, but unlike the 2011/12 grant, this will only be for one –year. The FRM assumes that this will be taken up by the council and used for one-off spending though a transformation fund.

5.9.4 The average Band D council tax for 2011/12 is £1.205.09, compared to the average Band D council tax for English Unitary authorities is £1,215.76.

5.9.5 Every 1% additional council tax raises £861k and costs taxpayers £12 per annum on a Band D property

5.10 Reserves

5.10.1 Revenue Reserves

5.10.2 Herefordshire has two main sources of reserve funding to support the day to day spending that is recorded in the revenue account, the General Fund balance and Specific Reserves. As the titles suggest, the latter are held for a specific purpose whilst the former could be considered a general contingency.

5.10.3 The following table shows the year end balance on the General Fund and the level of specific reserves for the last three financial years.

Balance as at:	General Fund £000	*Specific Reserves*		Total £000
		Schools	**Other**	
31st March 2009	6,359	5,476	17,472	29,307
31st March 2010	5,349	5,497	13,745	24,591
31st March 2011	6,349	6,002	11,570	23,921
31st March 2012 (est)	6,349	4,300	6,000	16,649

5.10.4 A significant proportion of the specific reserves belong to schools and cannot be used to help pay for non-schools services and unspent government grants carried forward in future years.

5.11 Managing the General Fund Balance and Specific Reserves

5.11.1 Herefordshire's General Fund opening balance for 2011/12 was £6.35m, which is in excess of the current policy in place to maintain a minimum balance of £4.5m (3%). The Chief Officer (Finance and Commercial Services) is content to make his statutory declaration that the minimum level of General Reserves is prudent.

5.11.2 Whilst the policy is for a general reserve of 3% it is considered prudent to use any amount in excess of 3% to fund a budget contingency.

5.11.3 Herefordshire's financial management strategy is to maintain specific reserves to deal with the key corporate financial risks reducing the need for a higher level of General Fund balances. This strategy ensures there is complete transparency about what is resourced, for corporate financial risks that, if realised, would affect the council's financial standing.

5.11.4 There is an increased level of risk attached to this volatile financial climate, and the use of these reserves is not advisable without a clear strategy for payback in a short timeframe.

5.11.5 All Directorates are expected to manage budget pressures within the overall requirement to deliver an outturn at or below budget. Any in-year budget pressures must be managed by use of a recovery plan, which is approved at HPSLT.

5.11.6 The need for the range and level of specific reserves and the policy for minimum General Fund balances is continually reviewed as part of the financial planning, monitoring and outturn processes.

5.12 Capital Reserves

5.12.1 There is one capital reserve that represents cash available to support spending on the creation or enhancement of assets that is recorded in the capital account. It is known as the Usable Capital Receipts Reserve. The following table shows the level of usable capital receipts for the last 4 financial years and an estimate for 2011/12;

Balance as at:	£000
31st March 2009	17,827
31st March 2010	13,565
31st March 2011	6,754
31st March 2012 (est)	3,547

5.12.2 The council has a policy that ensures capital cash resources are used effectively in support of corporate priorities. As a result all capital receipts are a corporate resource and not 'owned' or earmarked for directorates unless allocated for a specific purpose.

5.13.1 Funding Arrangements for Capital Investment

5.13.1 Capital expenditure can be funded from capital receipts, borrowing, grants and revenue contributions.

5.13.2 Government support for capital investment is through the allocation of grants and it no longer issues supported borrowing allocations. Known grant funding allocations for 2012/13 are:

Local Transport Plan

- This has been reduced by a further 5% to £10m for 2012/13 split between integrated transport and capital maintenance allocations. Indications are this funding will fall further to £9.8m for 2013/14 and 2014/15.

- Hereford submitted a successful application, Destination Hereford, for capital funding from the Local Sustainable Transport Fund, for sustainable transport initiatives in Hereford. £3.2m of grant funding is expected to be spent between 2012/13 and 2014/15 on improving Broad Street and providing the non-motorised connection between the city centre and Rotherwas.

Schools Capital

- There have been further substantial changes in the allocation of schools capital funding for 2012/13 due to a number of Herefordshire's schools converting to academies in 2011/12 and changes to the formula mechanisms that the DfE use to allocate capital grant funding.

- The total allocation for maintenance and basic need has reduced by 46% from an allocation of £4.8m in 2011/12 to £2.6m in 2012/13. Capital maintenance funding has been reduced by £0.9m; a separate funding pot is available for academies to bid for funding. Basic need funding has reduced by £1.3m as a result of funding formula changes from allocations being based on pupil growth and capacity in 2012/13 as opposed to being based on pupil growth alone in 2011/12. Further basic need funding available to central government is yet to be allocated. These allocations will be announced in the New Year along with the results of the priority school building review and response to the capital review carried out earlier in the year.

Adult Social Care

- The Department of Health has announced funding of £0.46m towards personalisation, reform and efficiency in adult social care in 2012/13.

Other Capital Grants

- Herefordshire has been selected as one of four pilot schemes to deliver superfast broadband to rural areas in Herefordshire and Gloucestershire, the procurement process is underway with the successful provider expected to be announced in May. The scheme is to be funded through grants from BDUK, Gloucestershire and corporate match funding.

- Herefordshire Council will receive £1.5m from the Regional Growth Fund for a new Marches Redundant Building Grant Scheme covering the 3 local authority areas in the Marches Local Enterprise Partnership (Herefordshire, Shropshire and Telford & Wrekin).

- Capital grant applications for funding towards the Masters House in Ledbury are to be confirmed, if successful this will enable the completion of the desired scheme.

5.13.3 **Council Borrowing** - The medium-term strategy reflects the borrowing requirement implied by the Treasury Management Strategy to support the capital programme currently in place and headroom has also been provided for to enable the allocation of capital funding to known capital budget pressures. Capital schemes that represent spend to save/mitigate, demonstrating a clear benefit are also likely to be allocated funding.

5.13.4 **Capital Receipts Reserve -** totalled £6.75m as at 1st April, 2011, this is likely to fall to around £3.5m by the end of the financial year. Capital receipts reserve funding has been committed to fund the capital programme in coming years.

5.13.5 **Other Funding opportunities -** The financial management strategy for increasing capital investment capacity centres on:

- **Maximising Developers' Contributions** – through planning gains and the adoption of a Community Infrastructure Levy.

- **Growing Places Fund –** this fund is welcoming bids from Local Enterprise Partnerships to quickly restart stalled infrastructure projects that promote the delivery of jobs & housing, prioritise infrastructure needs and establish a revolving fund to enable future reinvestment and lever in private funding.

- **External Funding Bodies** - Distribute funding for projects that satisfy their key criteria and objectives and bids are submitted where appropriate.

5.13.6 The challenges given to retaining assets will be based on value for money and the delivery of strategic priorities and key service delivery. Surplus properties will either be recycled or disposed of and proceeds will be reinvested. The disposal of land will be allowed after consideration of sacrificing a capital receipt for transfer of the land for use as social housing or as a community asset transfer.

5.13.7 Over the longer term authorities are expected to generate income from selling surplus assets and reduce the costs of running their property portfolios by providing efficiencies including reducing carbon emissions from their capital stock. At the same time there is increasing pressure to provide cross-cutting co-located services to provide a one-stop service provision to the public which is steering authorities to share buildings, pool resources and jointly plan strategic capital programmes with local agencies, private companies, voluntary sector and community organisations. For local authorities to deliver their priorities within the financial constraints officers must demonstrate creativity using greater innovation and ideas, to deliver services differently.

5.13.8 The localities agenda is steering authorities to share buildings, pool resources and jointly plan strategic capital programmes with local agencies, private companies, and voluntary sector and community organisations. This new concept of meaningful engagement at a very local level, critically challenges the historical basis for resource allocation and the effectiveness of services to deliver on local need and is designed to provide a more creative use of the current asset base and support improvements to community based planning and service. This is designed to produce more efficient local spending by pooling budgets and ending duplication.

5.14 Capital Programme 2012/13 to 2015/16

5.14.1 The 2012/13 capital programme represents funding indications received to date from grants, existing schemes that commenced in prior years and an allocation of corporate borrowing funded in the FRM but yet to be allocated to capital schemes.

5.14.2 A number of capital budget priorities have been identified, which link to the Capital Strategy.

5.14.3 The following business cases have been presented to the Capital Strategy Working Group ;

- Hereford Link Road

- Plough Lane refurbishment, data centre replacement and archive / MRU provision

- Herefordshire Broadband match funding

- Gas control works at Stretton Sugwas closed landfill site

5.14.4 The draft capital programme also includes funding of £1m for repairs to Garrick House car park. This will ensure it continues to provide income and parking capacity for those shopping in Hereford City Centre.

5.14.5 The following table summarises the existing capital investment programme;-

	2012/13	2013/14	2014/15	2015/16
Directorate	**£'000**	**£'000**	**£'000**	**£'000**
People's Services	12,828	-	-	-
Places & Communities	17,591	16,917	10,842	-
Corporate Services	4,351	12,257	-	-
Funding to be allocated	4,260	11,200	11,492	6,213
Contingency	*332*	*330*	*283*	-
TOTAL	**39,362**	**40,704**	**22,617**	**6,213**
Funded by				
Prudential Borrowing	11,905	23,787	11,775	6,213
Capital receipts reserve	465	70	-	-
Grants and contributions	26,992	16,847	10,842	-
TOTAL	**39,362**	**40,704**	**22,617**	**6,213**

5.15 Treasury Management Strategy

5.15.1 The council is required to approve an annual treasury management strategy each year as part of the budget setting process. Herefordshire's Treasury Management Strategy for 2012/13 is provided at Appendix A and complies with the detailed regulations that have to be followed.

5.15.2 The Treasury Management Strategy is a key element of the overall financial management strategy. It supports the achievement of several corporate financial objectives, including creating financial capacity within the revenue account as it aims to optimise investment and borrowing decisions.

5.15.3 In summary, the Treasury Management Strategy sets out the council's strategy for making borrowing and investment decisions during the year in the light of its view on future interest rates. It identifies the types of investment the council will use and the limits for non-specified investments. On the borrowing side, it deals with the balance of fixed to variable rate loan instruments, debt maturity profiles and rescheduling opportunities. The strategy also included the Minimum Revenue Provision (MRP) policy.

5.15.4 Since the 'credit crunch' a more cautious approach to investment has been implemented, these options deliver lower interest rates, but within a low risk environment. This approach, together with a historically low base rate, has resulted in reduced interest on investments used to support council budgets.

5.15.4 The council's treasury adviser assists the council in formulating views on interest rates. They are predicting that the bank base rate may well remain at 0.50% until 2015, keeping investment returns low for the foreseeable future.

5.15.5 On the borrowing side, PWLB rates are expected to move slowly upwards with short-term loans increasing by an estimated 0.25% over the course of 2012 and longer term loans by an estimated 0.45%.

5.15.6 The Treasury Management Strategy also sets the Prudential Code limits for the year and beyond. These limits define the framework within which the council self-regulates its borrowing based on long-term affordability. These link back to the overall size of the capital investment programme and the FRM.

5.15.7 The Treasury Management Strategy allows a pragmatic approach to the timing of borrowing. Due to low investment returns and the shortage of good quality counterparties to invest with, the council may postpone borrowing by running down its invested reserves, thus reducing risk and the costs of borrowing. However, it may be prudent to lock in low-rate loans, as the long-term savings from borrowing sooner rather than later, may out-weigh the benefits from further postponement.

5.16 Key Corporate & Financial Risks

5.16.1 HPS sees risk management as an essential element of the corporate governance framework. All formal reports include a risk management assessment.

5.16.2 Service Plans for each directorate provide a section on risk, assessing the feasibility of delivering their objectives against barriers for delivery.

5.16.3 The delivery of a balanced budget in 2012/13 and future years is a significant challenge, requiring close scrutiny of the proposed savings and at what point those savings are realised. The Benefits Board will be used to ensure a project management approach is adopted for the larger reductions, and monitor their progress to ensure the savings targets are delivered as planned.

6. Medium-Term Financial Resource Model (FRM)

6.1 Background

6.1.1 The FRM shown in Appendix B takes into account the corporate financial objectives and approach set out in this document. The FRM is designed to provide an assessment of the overall resource availability for the revenue account over the medium-term. It sets the financial context for corporate and service planning so that the two planning processes are fully integrated. It covers the period from 2012 to 2015.

6.2 Assumptions

6.2.1 The FRM includes the following assumptions;

a) **Council Tax** - a nil increase for 2012/13 and 2.5% there-after

b) **Formula Grant** – the FRM reflects the two year settlement, including the grants transferred in, plus an estimated further reduction in funding for 2014/15 and 2015/16.

c) **New Homes Bonus –** the provisional 2012/13 allocation for Herefordshire is £824k, giving a total of £1.4m for the 2 years of the scheme. A similar level of growth has been anticipated for future years.

d) **Inflation** -the current FRM includes 2% inflationary uplift on non pay expenditure and income

e) **Pay** – zero pay awards are assumed for 2011 and 2012, with 1% in the following years.

f) **Employers' superannuation costs** – the FRM includes increases in employers' contributions rates of 0.7% on gross pay in line with latest valuation which concluded in November.

g) **Interest Rates** – the FRM reflects interest rate assumptions for investment income and borrowing costs in line with the Treasury Management Strategy 2012/13.

6.3 Budget Process

6.3.1 The FRM includes key growth items and budget pressures identified as corporate priorities, alongside service and initiatives council wide to deliver savings.

6.3.2 Given the current settlement only covers two years (2011/12 and 2012/13) more detailed financial planning beyond that is difficult. The system of funding will change in 2013/14 to one based on the retention of business rates. The Government has stated that councils should be no worse off in the first year than they would have been under the current system. 2013/14 also sees changes in the funding of council tax and housing benefits and the transfer of public health responsibilities to councils.

2011/12

6.3.3 As the settlement announced in 2010 was worse in terms of total grant reduction and phasing Directors undertook work at that time to a further set of principles to help refine the budget proposals;

- Grant reductions were managed within Directorates.
- Budget growth was funded within Directorates.
- The additional sums provided for Adult Social Care as part of the settlement and also via Health was added to the overall control total for Adult Services.
- No additional capital borrowing in 2011 apart from agreed prior year decisions that still have a sound business case or where borrowing commitments cover projects already being delivered.
- Inflation was applied to budgets, including fees and charges

6.3.4 A Star Chamber process was used to identify and challenge savings proposals and service pressures in setting the budget for 2011/12. Proposals from each Directorate for further savings and service change based on the application of the Core Principles and Priorities of Valued Services, Cutting Red tape, Supporting the Vulnerable, Cutting Costs, Local Delivery and Personal Responsibility.

PRINCIPLE	IMPACT
Valued Services	• *Focusing on our priorities & what matters to people, stopping things we don't need to do*
Reducing Bureaucracy	• *Less regulation and red tape, smaller local government; right first time delivery*
Supporting the Vulnerable	• *Targeting resources on individuals, families, communities at risk or disadvantaged; early intervention & prevention; a shift in social care provision*
Value for Money	• *Reducing the pay bill; third party spend savings; smarter delivery; cutting costs*
Local Delivery	• *Devolution to parishes and the VCS, local decision making; working through 9 localities*
Personal Responsibility	• *Self reliance, people and communities helping themselves, behavioural change; increase in personalisation*

2012/13

6.3.5 The provisional local government finance settlement announced in December 2011 confirmed the formula grant funding for 2012/13 of £54.462m (increased to £56.615m by the inclusion of the second year of council tax freeze grant relating to 2011/12), a cash reduction of £5.7m (9.5%).

6.3.6 The Chancellor of the Exchequer has announced that Government will pay a grant to authorities which freeze their council tax for 2012/13. This grant is for one year only and optional for councils. By accepting the grant rather than increasing council tax by the same amount means losing the base effect of a

2.5% council tax increase. The FRM assumes this grant will be used for one-off funding for transformation in 2012/13.

6.3.7 Star Chambers were held in December 2011 to;
- confirm savings targets already included in the FRM
- Explore opportunities for further savings to balance the budget
- Discuss pressures and mitigating actions

6.4 Directorate pressures

6.4.1 Following the 2010 Star Chambers a number of the directorate pressures were included in the FRM, as shown below. These pressures relate to growth in demographics activity alongside specific contract inflation obligations. Any further growth will have to be self-funded by directorates.

Directorate	2011/12	2012/13
	£'000	£'000
People	885	**1,616**
Places and Communities	960	**640**
Corporate	(36)*	**(20)**
Total	**1,809**	**2,236**

*Includes reversal of previous year's one-off pressure

6.5 Directorate Savings

6.5.1 As has been explained earlier, 2012/13 presents Directorates with a series of financial challenges and a requirement that they support the Council to deliver a balanced budget.

6.5.2 The original 2012/13 savings target was £6.1m for Directorates plus £638k for Shared Services projects (including Hoople). As part of the budget settling process these savings were confirmed and increased to £9,764m**.** These are in addition to the £10.3m savings in 2011/12.

6.5.3 The FRM includes the following savings targets;

DIRECTORATE	ORIGINAL 2012/13 SAVINGS £'000	REVISED SAVINGS £'000
Corporate	**1,191**	**1,256**
Peoples	**3,500**	**4,324**
Places	**1,092**	**2,170**
Council Wide initiatives	**240**	**1,554**
TOTAL	**6,023**	**9,304**

6.6 Budget Engagement

6.6.1 Starting in November 2011 Herefordshire Public Services ran a series of events to ask local people for their views on funding priorities. This was done so that their feedback could help plan how its budget should be used for the coming year and beyond. With current pressures on funding being experienced by public services nationwide, it wanted to explore a new way of consulting the population at an early stage in the process. As a result, a series of 10 public events were held across the range of localities in the county during November and December 2011, attended by over 250 people in total. Alternatively, the public were able to send responses through an on-line questionnaire.

6.6.2 The consultation included four topic areas, on which people were asked a series of high-level questions about general spending principles on which each could cast their vote using an electronic hand-held device. Each section was first introduced by providing some contextual information. Questions were asked concerning finance, adult social care, clinical commissioning of healthcare, and health and wellbeing. This was followed by an opportunity for people to provide further comment and to ask questions of the presenters. The public also were also invited to complete an evaluation questionnaire to gather feedback on the events and this will help shape future consultations.

6.6.3 The headline feedback showed support for:

- Prioritising funding for services for vulnerable people
- The council not providing some services if it meant being able to protect and develop others
- Getting other organisations to provide some council functions
- Increasing support for access to services on-line
- Getting areas to be involved in delivering services
- Transferring assets to local groups to deliver services of benefit to the community

6.6.4 In addition more people agreed than disagreed that they would be willing to pay more council tax if it protected services.

7. Statutory Statement by the Council's Chief Finance Officer

7.1 The purpose of this statement is to comply with the requirements of the Local Government Act 2003 whereby the Chief Finance Officer, in the Council's case the Chief Officer (Finance and Commercial) must report on the:

a) Robustness of the estimates made for the purposes of the budget calculations.

b) Adequacy of the proposed financial reserves.

7.2 Section 25 of the Local Government Act 2003 requires the Chief Officer (Finance and Commercial) to report to the Council when it is setting the budget and precept (Council tax). The Council is required to take this report into account when making its budget and precept decision. The Chief Officer (Finance and Commercial)'s report must deal with the robustness of the estimates included in the budget and the adequacy of reserves.

7.3 The Chief Officer (Finance and Commercial) states that to the best of his knowledge and belief these budget calculations are robust and have full regard to:

- The council's corporate plans and strategies;
- The council's budget strategy;
- The need to protect the council's financial standing and manage corporate financial risks;
- This year's financial performance;
- The Government's financial policies;
- The council's medium-term financial planning framework;
- Capital programme obligations;
- Treasury Management best practice;
- The strengths of the council's financial control procedures;
- The extent of the council's balances and reserves; and
- Prevailing economic climate and future prospects.

David Powell
Chief Officer (Finance and Commercial)

Appendix A

Herefordshire Council

Treasury Management Strategy 2012/13

Contents

Appendices

1. Background

1.1 The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators on an annual basis. The TMSS also includes the Annual Investment Strategy as required under Investment Guidance provided by Communities and Local Government (CLG).

1.2 CIPFA has defined Treasury Management as:

"the management of the organisation's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

1.3 Treasury Management is about the management of risk. The council is responsible for its treasury decisions and activity. No treasury management activity is without risk.

1.4 The purpose of this TMSS is to approve:

- Treasury Management Strategy for 2012/13 (Borrowing and Debt Rescheduling – Section 3 and Investments and Annual Investment Strategy – Section 4)
- MRP Statement – Section 6
- Prudential Indicators (Appendix 2)
- Use of Specified and Non-Specified Investments – Appendices 4 & 5

1.5 As per the requirements of the Prudential Code, the council has adopted the CIPFA Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. The aim is to ensure that treasury management is led by a clear and integrated forward treasury management strategy, and a recognition of the pre-existing structure of the authority's borrowing and investment portfolios.

1.6 All treasury activity will comply with relevant statute, guidance and accounting standards.

2. Capital Financing Requirement

2.1 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). The CFR, together with Usable Reserves, are the core drivers of treasury management activity. The estimates, based on the current revenue budget and capital programme, are as follows:

Balance Sheet Summary Analysis				
	31/03/2012 Estimate £'000	**31/03/2013 Estimate £'000**	**31/03/2014 Estimate £'000**	**31/03/2015 Estimate £'000**
Capital Financing Requirement	**208,208**	**209,189**	**222,311**	**222,956**
LESS:				
Existing Profile of Borrowing	147,516	143,382	139,235	**135,073**
Other Long Term Liabilities	28,481	27,505	26,438	**25,296**
Cumulative Maximum External Borrowing Requirement	**32,211**	**38,302**	**56,638**	**62,587**
Usable Reserves	**32,024**	**31,000**	**30,000**	**29,000**
Cumulative Net Borrowing Requirement	**187**	**7,302**	**26,638**	**33,587**

2.2 The existing profile of borrowing above assumes that before the end of March 2012 the council will take out an additional £3 million 20 year EIP loan from the PWLB.

2.3 The council is able to borrow funds in excess of the current level of its CFR up to the projected level in 2014/15. The council may consider borrowing in advance of need if the benefits of borrowing at interest rates now, compared to where they are expected to be in the future, outweigh the current cost and risks associated with investing the funds until the borrowing is actually required.

2.4 The council's current level of debt and investments is set out at ***Appendix 1.***

3. Borrowing

Interest Rate Forecast

3.1 The economic and interest rate forecast provided by Arlingclose, the council's treasury management advisor, is attached at ***Appendix 3***. The council will reappraise its strategies from time to time in response to evolving economic, political and financial events.

Borrowing Strategy

3.2 Treasury management, and borrowing strategies in particular, continue to be influenced not only by the absolute level of borrowing rates but also the relationship between short and long term interest rates. The interest rate forecast provided in ***Appendix 3*** indicates that an acute difference between short and longer term interest rates is expected to continue. This difference creates a "cost of carry" for any new longer term borrowing where the proceeds are temporarily held as investments because of the difference between the interest rate paid on the borrowing and that earned on investments. Whilst the cost of carry can be assumed to be a reasonably short-term issue, since borrowing is often for longer dated periods (anything up to 50 years), it cannot be ignored against a backdrop of uncertainty and affordability constraints in the council's wider financial position.

3.3 As indicated in the table above, depending upon the actual movement in usable reserves, the council has a borrowing requirement in 2012/13 of between £6 and £7 million. The council will adopt a flexible approach to this borrowing in consultation with its treasury management advisers, Arlingclose Ltd. The following issues will be considered prior to undertaking any external borrowing:

- Affordability;
- Maturity profile of existing debt;
- Interest rate and refinancing risk;
- Borrowing source.

Sources of Borrowing and Portfolio implications

3.4 In conjunction with advice from its treasury advisor, Arlingclose, the council will keep under review the following borrowing sources:

- PWLB
- Local authorities
- Commercial banks
- European Investment Bank
- Money markets
- Capital markets (stock issues, bond issuance, commercial paper and bills)
- Structured finance (such as leasing etc)

3.5 The cost of carry has resulted in an increased reliance upon shorter dated borrowing. This type of borrowing injects volatility into the debt portfolio in terms of refinancing risk (the risk of having to refinance when interest rates are unfavourable) but is counterbalanced by its affordability and narrowing of the gap between borrowing costs and investment returns. At present all the council's borrowing is at fixed rates. With rates forecast to rise over the next few years the council has preferred to take out fixed rate loans rather than variable rate borrowing but this strategy will be kept under review.

3.6 The council has two LOBO loans (Lender's Option Borrower's Option) of £6 million each on which the council pays interest at 4.5%. Every year the lenders have the option to increase the interest rate being charged at which point the council can accept the revised terms or reject them and repay the loan. LOBO loans present a potential refinancing risk to the council since the decision to amend the terms is entirely at the lender's discretion.

3.7 If a lender seeks to amend the terms of a LOBO loan the available options will be discussed with the council's treasury advisers prior to acceptance of any revised terms. The default position will be the repayment of the LOBO without penalty i.e. the revised terms will not be accepted.

3.8 As interest rates are forecast to remain relatively low, it is considered unlikely that the lender will seek to vary the terms during 2012/13.

Debt Rescheduling

3.9 The council's debt portfolio can be restructured by prematurely repaying loans and refinancing them on similar or different terms to achieve a reduction in risk and/or interest savings.

3.10 The lower interest rate environment and changes in the rules regarding the premature repayment of PWLB loans has adversely affected the scope for debt restructuring although occasionally opportunities arise. The rationale for undertaking any debt rescheduling continues to be one or more of the following:

- Savings in interest costs with minimal risk
- Rebalancing the volatility profile (i.e. the ratio of fixed to variable rate debt) of the debt portfolio
- Changing the maturity profile of the debt portfolio to reduce refinancing risks.

3.11 Borrowing and rescheduling activity will be reported to Full Council in the annual end of year treasury management report and in the more regular treasury management reports presented to the Herefordshire Public Services Leadership Team and Cabinet.

4. Investments

Annual Investment Strategy

4.1 In accordance with Investment Guidance issued by the CLG and best practice the council's primary objective in relation to the investment of public funds remains the security of capital. Secondary objectives are the liquidity or accessibility of the council's investments followed by yield.

4.2 Credit markets remain in a state of distress as a result of the excessive and poor performing debt within the financial markets. In some instances, Greece and Italy being the most notable examples, the extent and implications of a country's indebtedness have led to a sovereign debt crisis and a more wider banking crisis with the outcome still largely unknown. It is against this backdrop of uncertainty that the council's investment strategy is framed.

4.3 Investments are categorised as "Specified" or "Non-Specified" within the investment guidance issued by the CLG.

Specified investments are sterling denominated investments with a maximum maturity of one year. They also meet the "high credit quality" as determined by the council and are not deemed capital expenditure investments under Statute. Non specified investments are, effectively, everything else.

4.4 The types of investments that may be used by the council and whether they are specified or non-specified are as follows:

Specified and Non-Specified Investments		
Investment	**Specified**	**Non-Specified**
Term deposits with banks and building societies	✓	✓
Term deposits with other UK local authorities	✓	✓
Certificates of deposit with banks and building societies	✓	✓
Gilts	✓	✓
Treasury Bills (T-Bills)	✓	N/a
Bonds issued by Multilateral Development Banks	✓	✓
Local Authority Bills	✓	N/a
Commercial Paper	✓	N/a
Corporate Bonds	✓	✓
AAA rated Money Market Funds	✓	N/a
Other Money Market and Collective Investment Schemes	✓	✓
Debt Management Account Deposit Facility	✓	N/a

N/a = This type of investment is not an option for longer-term deposits

4.5 A number of changes have been made to the investment strategy for 2012/13 in response to changes in the CLG Guidance and evolving conditions in financial markets. One change is the inclusion of corporate bonds which the CLG have indicated will become an eligible non-capital investment from 1st April 2012. However, the principal amendments are in relation to the individual institutions with which the Authority is prepared to lend its funds.

4.6 The council and its advisors, Arlingclose Ltd, select countries and financial institutions after analysis and ongoing monitoring of:

- Published credit ratings for financial institutions (minimum long term rating of A- or equivalent for counterparties; AA+ or equivalent for non-UK sovereigns) – this is lower than the A+ minimum adopted in the 2011/12 Strategy and is in response to downgrades in credit ratings below A+ of many institutions considered to be systemically important to the financial system.
- Credit Default Swaps (where quoted)
- Economic fundamentals (for example Net Debt as a percentage of GDP)
- Sovereign support mechanisms
- Share Prices
- Corporate developments, news, articles, markets sentiment and momentum
- Subjective overlay – or, put more simply, common sense.

Any institution can be suspended or removed should any of the factors identified above give rise to concern.

It remains the council's policy to make exceptions to counterparty policy established around credit ratings, but this is conditional and directional. What this means is that an institution that meets criteria may be suspended, but institutions not meeting criteria will not be added.

The Council's Bank

4.7 The council banks with National Westminster Bank. At the current time, it has a long-term credit rating of A so whilst it does not currently meet the minimum criteria for 2011/12 it will meet the revised criteria of A- for 2012/13. Even if the credit rating falls below the council's minimum criteria National Westminster Bank will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements.

Investment Strategy

4.8 With short term interest rates remaining low for even longer, an investment strategy will typically result in a lengthening of investment periods, where cash flow permits, in order to lock in higher rates of acceptable risk adjusted returns. The problem in the current environment is finding an investment counterparty providing acceptable levels of counterparty risk.

4.9 Investments will be placed in order to achieve a diversified portfolio of prudent counterparties, investment periods and rates of return. Maximum investment levels with each counterparty will be set to ensure prudent diversification is achieved.

4.10 Money market funds (MMFs) will be utilised but good treasury management practice prevails and whilst MMFs provide good diversification the council will also seek to diversify any exposure by utilising more than one MMF. The council will also restrict its exposure to MMFs with lower levels of funds under management and will not exceed 0.5% of the net asset value of the MMF.

4.11 <u>Collective Investment Schemes (Pooled Funds)</u>:

On the advice of Arlingclose Ltd, the council may consider using Pooled Funds. Pooled Funds would enable the council to diversify the assets and the underlying risk in the investment portfolio and provide the potential for enhanced returns.

4.12 Pooled Funds and Collective Investment Schemes currently recommended by Arlingclose are as follows:

- Cazenove UK Corporate Bond Fund
- City Financial Strategic Gilt Fund
- Elite Charteris Premium Income Fund
- Investec short Dated Bond Fund
- Investec Target Return Fund
- Investec UK Alpha Fund
- Payden & Rygel Sterling Reserve Fund
- Prime Rate Sterling Cash Plus Fund
- WAY Charteris Gold Portfolio Fund
- The Local Authorities Mutual Investment Trust – Property Fund
- Lime Property Fund

4.13 Pooled Funds are similar in nature to unit trusts in that they should be viewed as a longer term investment, there is an initial subscription fee and the value of the capital invested can go down as well as up. The council is not currently using any investments which do not guarantee the safe return of the principal invested, however, this option will remain under review.

5. Balanced Budget Requirement

5.1 The council complies with the provisions of S32 of the Local Government Finance Act 1992 to set a balanced budget.

6. 2012/13 MRP Statement

Background

6.1 For many years local authorities were required by Statute and associated Statutory Instruments to charge to the Revenue Account an annual provision for the repayment of debt associated with expenditure incurred on capital assets. This charge to the Revenue Account was referred to as the Minimum Revenue Provision (MRP). In practice MRP represents the financing of capital expenditure from the revenue account that was initially funded by borrowing.

6.2 In February 2008 the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 [Statutory Instrument 2008/414] were approved by Parliament and became effective on 31 March 2008. These regulations replaced the formula based method for calculating MRP which existed under previous regulations under the Local Government Act 2003. The new regulations require a local authority to determine each financial year an amount of MRP which it considers to be prudent. Linked to this new regulation, CLG produced Statutory Guidance which local authorities are required to follow, setting out what constitutes a prudent provision.

6.3 The CLG Guidance recommends that before the start of the financial year, a statement of MRP policy for the forthcoming financial year is approved by the Full Council.

6.4 The broad aim of the policy is to ensure that MRP is charged over a period that is reasonably commensurate with the period over which the capital expenditure (which gave rise to the debt) provides benefits. In the case of borrowing supported by Revenue Support Grant, the aim is that MRP is charged over a period reasonably commensurate with the period implicit in the determination of that grant.

6.5 The move to International Financial Reporting Standards (IFRS) means that Private Finance Initiative (PFI) schemes and finance leases have now been brought on Balance Sheet. Such items are classed in accounting terms as a form of borrowing. CLG has therefore amended the Capital Finance Regulations to ensure that the impact on the revenue account is neutral, with MRP for these items matching the principal repayment embedded within the PFI or lease agreement.

Options for making 'Prudent Provision'

6.6 There are four options for Prudent Provision set out in the guidance:

Option 1 - Regulatory

For debt which is supported by the Government through Revenue Support Grant (RSG), authorities may continue to use the formulae under the 2003 Regulations, as RSG debt support is calculated in that way. This includes applying an adjustment (the Item A adjustment), which reduces the charge back to the former credit ceiling accounting methodology.

Option 2 - CFR method

This is similar to option 1, but just uses the CFR and doesn't apply the full formula, including the Item A adjustment. Under this option the annual repayment would be higher.

Option 3 - Asset Life method

For new borrowing under the prudential system there are 2 options in the guidance. The first is to make provision over the estimated life of the asset for which the borrowing is undertaken. This can either be on an equal instalment method or an annuity basis.

Option 4 - Depreciation method

An alternative to Option 3 is to make provision in line with depreciation accounting. Although this would follow standard rules for depreciation accounting there would have to be some exceptions, for example, that MRP would continue until the provision is equal to the original debt and then cease.

MRP Policy 2012-13

6.7 In line with the guidance produced by the Secretary of State, the proposed policy for the 2012/13 calculation of MRP is as follows:

- Borrowing supported through the RSG grant system will be repaid in accordance with the 2003 Regulations.
- Prudential borrowing will be repaid over the life of the asset on an equal instalment basis commencing in the year following the year in which the asset first becomes operational.
- For expenditure under Regulation 25(1)(b), loans and grants towards capital expenditure by third parties, prudential borrowing will be repaid over the life of the asset in relation to which the third party expenditure is incurred.
- MRP in respect of PFI and leases brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability.

EXISTING DEBT & INVESTMENTS AS AT 31 DECEMBER 2011

	31/12/11 Actual Debt Position £'000
External Borrowing:	
Public Works Loan Board	130,597
Bank Loans	12,000
All loans are fixed rate loans	
Total External Borrowing	**142,597**

	31/12/11 Actual Debt Position £'000
Other Long Term Liabilities:	
- PFI	28,148
- Finance Leases	333
Total of Other Long Term Liabilities	**28,481**

	31/12/11 Actual Investments £'000
Investments:	
- Instant access Money Market Funds	13,520
- Short-term deposits	20,500
All investments are managed in-house	
Total Investments	**34,020**

PRUDENTIAL INDICATORS

1. Background:

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their Prudential Indicators.

2. Net Borrowing and the Capital Financing Requirement:

CIPFA refers to this indicator as a key indicator of prudence. In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that the net external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus the estimates of any additional increases to the capital financing requirement for the current and next two financial years.

The Chief Officer – Finance and Commercial reports that the council had no difficulty meeting this requirement in 2011/12, nor are there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

3. Estimates of Capital Expenditure:

3.1 This indicator is set to ensure that the level of proposed capital expenditure remains within sustainable limits and, in particular, to consider the impact on Council Tax.

Capital Expenditure	2011/12 Approved £'000	2011/12 Revised £'000	2012/13 Estimate £'000	2013/14 Estimate £'000	2014/15 Estimate £'000
Total	**55,477**	**57,918**	**39,362**	**40,704**	**22,617**

3.2 Capital expenditure will be financed or funded as follows:

Capital Financing	2011/12 Approved £'000	2011/12 Revised £'000	2012/13 Estimate £'000	2013/14 Estimate £'000	2014/15 Estimate £'000
Capital receipts	4,260	4,589	465	70	0
Government Grants	40,297	42,739	26,992	16,847	10,842
Total Financing	**44,557**	**47,328**	**27,457**	**16,917**	**10,842**
Prudential borrowing	**10,920**	**10,590**	**11,905**	**23,787**	**11,775**
Total Financing and	**55,477**	**57,918**	**39,362**	**40,704**	**22,617**

Funding					

4. Ratio of Financing Costs to Net Revenue Stream:

4.1 This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs.

4.2 The ratio is based on costs net of investment income.

Ratio of Financing Costs to Net Revenue Stream	**2011/12 Approved £'000**	**2011/12 Revised £'000**	**2012/13 Estimate £'000**	**2013/14 Estimate £'000**	**2014/15 Estimate £'000**
Net Revenue Stream	146,248	146,314	**143,359**	144,095	144,969
Financing Costs	17,833	17,311	**18,049**	18,018	18,781
Percentage	**12.19%**	**11.83%**	**12.59%**	**12.50%**	**12.96%**

5. Capital Financing Requirement:

5.1 The Capital Financing Requirement (CFR) measures the council's underlying need to borrow for a capital purpose. The calculation of the CFR is taken from the amounts held in the Balance Sheet relating to capital expenditure and its financing.

Capital Financing Requirement	**2011/12 Approved £'000**	**2011/12 Revised £'000**	**2012/13 Estimate £'000**	**2013/14 Estimate £'000**	**2014/15 Estimate £'000**
Total CFR	**209,550**	**208,208**	**209,189**	**222,311**	**222,956**

6. Actual External Debt:

6.1 This indicator is obtained directly from the council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities. This indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

Actual External Debt as at 31/03/2011	**£'000**
Borrowing (including £5.5 million of short-term loans)	147,035
Other Long-term Liabilities – Finance leases and PFI schemes	29,390
Total	**176,425**

7. Incremental Impact of Capital Investment Decisions:

7.1 This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax levels. The incremental impact is calculated by comparing the total revenue budget requirement of the current approved capital programme with an equivalent calculation of the revenue budget requirement arising from the proposed capital programme.

Incremental Impact of Capital Investment Decisions	**2012/13 Estimate £'000**	**2013/14 Estimate £'000**	**2014/15 Estimate £'000**
New capital expenditure funded by Prudential borrowing	**4,200**	**11,200**	**11,492**
Interest payable	84	406	903
MRP - Provision for repayment of principal over 25 years (commencing year after expenditure incurred)	0	168	616
Total financing costs	84	574	1,519
Estimated taxbase	71,982	72,342	72,703
	£	**£**	**£**
Increase in Band D Council Tax (Currently £1,205.09 for 2011/12)	**1.17**	**7.93**	**20.89**

7.2 The above increase in Band D council tax reflects the increase in the provision for capital financing charges arising from the proposed capital programme. The interest payable is calculated assuming that the supporting loans are taken out mid-year at rates ranging from 4.00% to 4.50%.

7.3 An increase in capital financing charges does not necessarily mean that council tax will be increased by an equivalent amount due to savings in other areas. For example, no increase is planned to council tax for 2012/13.

8. Authorised Limit and Operational Boundary for External Debt:

8.1 The Council has an integrated treasury management strategy and manages its treasury position in accordance with its approved strategy and practice. Overall borrowing will therefore arise as a consequence of all the financial transactions of the Council and not just those arising from capital spending reflected in the CFR.

8.2 The **Authorised Limit** sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities). This Prudential Indicator separately identifies borrowing from other long term liabilities such as finance leases. It is consistent with the Council's existing commitments, its proposals for capital expenditure and financing and its approved treasury management policy statement and practices.

8.3 The Authorised Limit has been set on the estimate of the most likely, prudent but not worst case scenario with sufficient headroom over and above this to allow for unusual cash movements.

8.4 The Authorised Limit is the statutory limit determined under Section 3(1) of the Local Government Act 2003 (referred to in the legislation as the Affordable Limit).

Authorised Limit for External Debt	**2011/12 Approved £m**	**2011/12 Revised £m**	**2012/13 Estimate £m**	**2013/14 Estimate £m**	**2014/15 Estimate £m**
Borrowing	190	190	**185**	195	195
Other Long-term Liabilities	40	40	**40**	40	40
Total	**230**	**230**	**225**	**235**	**235**

8.5 The Operational Boundary links directly to the council's estimates of the CFR and estimates of other cashflow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely, prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

8.6 The Chief Officer – Finance and Commercial has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next meeting of Full Council.

Operational Boundary for External Debt	2011/12 Approved £m	2011/12 Revised £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Borrowing	175	175	**175**	190	190
Other Long-term Liabilities	35	35	**35**	35	35
Total	**210**	**210**	**210**	**225**	**225**

9. Adoption of the CIPFA Treasury Management Code:

9.1 This indicator demonstrates that the Council has adopted the principles of best practice.

9.2 The Council has incorporated the changes from the revised CIPFA Code of Practice into its treasury policies, procedures and practices. The council's Treasury Management Policy Statement is attached at **Appendix 6**.

10. Gross and Net Debt:

10.1 The purpose of this treasury indicator is to highlight a situation where the council is planning to borrow in advance of need.

Gross and Net Debt	2011/12 Estimated £m	2012/13 Estimated £m	2013/14 Estimated £m	2014/15 Estimated £m
Outstanding Borrowing (at nominal value)	148	152	**166**	168
Other Long-term Liabilities (at nominal value)	28	28	**26**	25
Gross Debt	176	178	**192**	193
Less:Investments	20	20	**20**	20
Net Debt	**156**	**160**	**172**	**173**

11. Upper Limits for Fixed Interest Rate Exposure and Variable Interest Rate Exposure

11.1 This indicator allows the council to manage the extent to which it is exposed to changes in interest rates.

11.2 The upper limit for variable rate exposure has been set to ensure that the council is not exposed to interest rate rises which could adversely impact on the revenue budget. The limit allows for the use of variable rate debt to offset exposure to changes in short-term rates on investments

	2011/12	2011/12	2012/13	2013/14	2014/15

	Approved %	Revised %	Estimate %	Estimat e %	Estimate %
Upper Limit for Fixed Interest Rate Exposure	**100%**	**100%**	**100%**	**100%**	**100%**
Upper Limit for Variable Interest Rate Exposure	**25%**	**25%**	**25%**	**25%**	**25%**

11.3 The limits above provide the necessary flexibility within which decisions will be made for drawing down new loans on a fixed or variable rate basis; the decisions will ultimately be determined by expectations of anticipated interest rate movements.

11.4 The council's borrowing currently relates wholly to fixed interest rate loans. However, it is recognised that it may be desirable to have a variable element in the loans portfolio over the longer term (particularly when interest rates are high or falling) and so the council continues to monitor rates and will take out variable borrowing when it is considered advantageous to do so.

12. Maturity Structure of Fixed Rate borrowing:

12.1 The council will also limit and monitor large concentrations of fixed rate debt needing to be replaced. Limits in the following table are intended to control excessive exposures to volatility in interest rates when refinancing maturing debt.

12.2 The maturity of borrowing is determined by reference to the earliest date on which the loans could be repaid. Therefore the council's two LOBO loans are included as being repayable within 12 months although, if the lenders do not increase the interest rates being charged, the loans could remain outstanding until 2054.

Maturity structure of fixed rate borrowing	Estimated level as at 31/03/12 %	Lower Limit for 2012/13 %	Upper Limit for 2012/13 %
Under 12 months (including LOBO's)	11%	0%	20%
12 months and within 24 months	3%	0%	10%
24 months and within 5 years	14%	0%	30%
5 years and within 10 years	12%	0%	30%
10 years and within 20 years	26%	0%	40%
20 years and within 30 years	12%	0%	40%
30 years and within 40 years	7%	0%	40%
40 years and within 50 years	15%	0%	40%
Total	100%		

13. Credit Risk:

13.1 The council considers security, liquidity and yield, in that order, when making investment decisions.

13.2 Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in the council's assessment of counterparty credit risk.

13.3 The council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution (minimum A- or equivalent) and its sovereign (minimum AA+ or equivalent for non-UK sovereigns);
- Sovereign support mechanisms;
- Credit default swaps (where quoted);
- Share prices (where available);
- Economic fundamentals, such as a country's net debt as a percentage of its GDP);
- Corporate developments, news, articles, markets sentiment and momentum;
- Subjective overlay.

13.4 Credit ratings remain the only indicators with prescriptive values. Other indicators of creditworthiness are considered in relative rather than absolute terms.

14. Upper Limit for total principal sums invested over 364 days:

14.1 The purpose of this limit is to contain exposure to the possibility of loss that may arise as a result of the council having to seek early repayment of the sums invested.

Upper Limit for total principal sums invested over 364 days	2011/12 Approved £'000	2011/12 Revised £'000	2012/13 Estimate £'000	2013/14 Estimate £'000	2014/15 Estimate £'000
	10,000	**10,000**	**15,000**	**15,000**	**15,000**

OUTLOOK FOR INTEREST RATES
(FORECAST & ECONOMIC COMMENT PROVIDED BY ARLINGCLOSE)

	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14
Bank Base Rate (%)	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
PWLB Rates (%):													
5 years	2.25	2.30	2.35	2.40	2.50	2.60	2.70	2.80	3.00	3.10	3.30	3.40	3.50
10 years	3.20	3.30	3.40	3.45	3.50	3.55	3.60	3.70	3.75	3.80	3.85	3.90	4.00
20 years	4.00	4.05	4.05	4.10	4.20	4.25	4.30	4.35	4.40	4.45	4.50	4.60	4.75
50 years	4.25	4.40	4.50	4.60	4.70	4.80	4.90	5.00	5.00	5.00	5.10	5.20	5.25
The above PWLB rates are noted by Arlingclose as their "central" or most likely forecast, however, they also note that they could be up to 0.50% higher or up to 0.25% lower than the above.													

- Whilst the financial crisis in the Eurozone continues, the UK's status as a safe haven remains and keeps Gilt yields (and hence PWLB rates) supressed.
- Conventional monetary policy has become largely redundant; the Bank of England and the US Federal Reserve have signalled their respective official interest rates will be on hold through to the end of 2012. Arlingclose think that it could be 2016 before official interest rates rise.
- The Bank of England's Monetary Policy Committee embarked on a further round of Quantitative Easing (QE). The view is there will be more to come.

Underlying Assumptions:

- Arlingclose believe that stress in financial markets continues to build. Rates within Interbank markets (where banks fund the majority of their day to day operations) continue to climb. This situation was a feature of the banking crisis that occurred in 2008 and, whilst the authorities have flooded the markets with liquidity (quantitative easing), it still provides a key barometer of rising risk within markets.
- The MPC's decision to embark on a further £75 billion of QE – which the Minutes showed was unanimously supported – is likely to be expanded in the coming months as some members of the MPC had voted for £100bn of QE.
- Inflation fell back to 5% from what is considered to be its peak of 5.2% reached in October 2011. The Bank of England expects domestic inflation to subside

markedly in 2012 as the twin effects of the VAT increase and surge in oil prices fall out of the twelve month series.

- Economic growth meanwhile remains largely illusive not helped by the considerable uncertainty and expansion of risks presented by the crisis in the Eurozone. Even if a credible and effective policy is implemented, the scale of the problems mean that there is likely to be a prolonged period of subdued growth within the Euro area. A failure to meet the challenges would almost certainly have significant implications for the global economy.
- Recent data and surveys suggest that the UK economy has lost the admittedly fragile momentum since the summer. Business and consumer surveys point to continued weakness in coming months and the situation in the Euro area is likely to further undermine confidence and lead to tighter credit conditions for households and firms.
- Against this uncertain backdrop the ability of the economy (government, companies and individual consumers) to accommodate an increase in the cost of money through higher interest rates – in the absence of a deterioration in the high credit standing that the UK enjoys – remains unlikely. In fact, we believe that it is highly unlikely.

APPENDIX 4

SPECIFIED INVESTMENTS FOR USE BY THE COUNCIL

Specified Investments will be those that meet the criteria in the CLG Guidance, i.e. the investment:

- is sterling denominated
- has a maximum maturity of 1 year
- meets the “high credit quality” as determined by the council or is made with the UK government or is made with a local authority in England, Wales, Scotland or Northern Ireland or a parish or community council.
- the making of which is not defined as capital expenditure under section 25(1)(d) in SI 2003 No 3146 (i.e. the investment is not loan capital or share capital in a body corporate).

“Specified” Investments identified for the council’s use are:

- Term deposits with banks and building societies
- Term deposits with other UK local authorities
- Certificates of deposit (CD’s) with banks and building societies
- Gilts: (bonds issued by the UK government)
- Treasury Bills
- Bonds issued by multilateral development banks
- Local Authority Bills
- Commercial Paper
- Corporate Bonds
- AAA-rated Money Market Funds with a Constant Net Asset Value (CNAV)
- AAA-rated Money Market Funds with a Variable Net Asset Value (VNAV)
- Other Money Market Funds and Collective Investment Schemes– i.e. credit rated funds which meet the definition of a collective investment scheme as defined in SI 2004 No 534 and SI 2007 No 573.
- Deposits in the DMO’s Debt Management Account Deposit Facility

For credit rated counterparties, the minimum criteria will be the lowest equivalent short-term and long-term ratings assigned by Fitch, Moody’s and Standard & Poor’s (where assigned).

Long-term minimum: A- (Fitch); A3 (Moody’s;) A- (S&P)
Short-term minimum: F1 (Fitch); P-1 (Moody’s); A-1 (S&P)

The table below shows the complete list of long term credit ratings highlighting those considered acceptable in 2012/13. The short term credit ratings are only examples and the table does not show all the possible combinations of the long and short term ratings that may exist.

Long Term Credit Ratings – Audit Commission Gradings						
	Fitch		**Moody's**		**Standard and Poor's**	
	Long term	**Short term**	**Long term**	**Short term**	**Long term**	Short term
Extremely strong	AAA	F1+	Aaa	P-1	AAA	A-1+
Very strong grade	AA+	F1+	Aa1	P-1	AA+	A-1+
	AA	F1+	Aa2	P-1	AA	A-1+
	AA-	F1+	Aa3	P-1	AA-	A-1+
Strong grade (But susceptible to adverse conditions)	A+	F1+ or	A1	P-1	A+	A-1+ or A-1
	A	F1	A2	P-1 or P-2	A	A-1+
	A-	F1 or F2	A3	P-1 or P-2	A	A-1+ or A-2
Adequate grade	BBB+	F2	Baa1	P-2	BBB+	A-2
	BBB	F2 or F3	Baa2	P-2 or P-3	BBB	A-2 or A-3
	BBB-	F3	Baa3	P-3	BBB-	A-3
Speculative grade	BB+	B	Ba1	NP (Not Prime)	BB+	B-1
	BB	B	Ba2	NP	BB	B-2
	BB-	B	Ba3	NP	BB-	B-3
Very speculative grade	B+	B	B1	NP	B+	-
	B	B	B2	NP	B	-
	B-	B	B3	NP	B-	-
Vulnerable grade	CCC	C	Caa1	NP	CCC+	C
	CCC	C	Caa2	NP	CCC	C
	CCC	C	Caa3	NP	CCC-	C
	CC	C	-	NP	CC	C
	C	C	Ca	NP	C	C
Defaulting grade	D	D	C	NP	D	D

The council will also take into account information on corporate developments and market sentiment towards investment counterparties.

New specified investments may be made within the following limits:

Instrument	Country/ Domicile	Counterparty	Maximum Counter-party Limits £m
Term Deposits	UK	Other UK Local Authorities	No limit
Term Deposits, CDs & Call Accounts	UK	Counterparties rated at least A- Long Term and F1 Short Term (or equivalent)	£5m or 15%, whichever is greater
Term Deposits, CDs & Call Accounts	Non-UK	Counterparties rated at least A- Long Term and F1 Short Term (or equivalent) in select countries with a Sovereign Rating of at least AA+	£5m or 15%, whichever is greater
Corporate Bonds	UK	Counterparties rated at least A- Long Term and F1 Short Term (or equivalent)	£5m or 15%, whichever is greater
Gilts	UK	DMO	No limit
Treasury Bills	UK	DMO	No limit
Bonds issued by multilateral development banks		(For example, European Investment Bank/council of Europe, Inter American Development Bank)	£5m or 15%, whichever is greater
Local Authority Bills	UK	Other UK local authorities	No limit
Commercial Paper	UK and Non-UK	Corporates where the issue is rated at least F1 short-term	£5m or 15%, whichever is greater
AAA-rated Money Market Funds	UK/Ireland/ Luxembourg domiciled	CNAV MMFs VNAV MMFs (where there is greater than 12 month history of a consistent £1 Net Asset Value)	£5m or 15%, whichever is greater – Limit applied per Fund
Other MMFs and Collective Investment Schemes	UK/Ireland/ Luxembourg domiciled	Pooled funds which meet the definition of a Collective Investment Scheme per SI 2004 No 534 and subsequent amendments	£5m or 15%, whichever is greater – Limit applied per Fund
Term Deposits	UK	Debt Management Office	No limit

NB

The limit of 15% relates to the proportion invested with that counterparty as a percentage of the council's total investments and, in the case of term deposits, the limit is applied at the time the investment is made.

In the case of call accounts the 15% limit will be calculated on a monthly basis. The limit for each month will be fixed by taking 15% of the average total investments for the previous month.

Group Limits - For institutions within a banking group, a limit of 1.5 times the individual limit of a single bank within that group is used. For example, a single bank may have a limit of 15% but if it is part of a group an overall group limit of 22.5% will be applied.

Non-UK Banks - These will be restricted to a maximum exposure of 25% per country to limit the risk of over-exposure to any one country.

MMFs – Arlingclose emphasise diversification for all investments including MMFs and so the council will spread their investments in Money Market Funds between two or more Funds.

APPENDIX 5

NON-SPECIFIED INVESTMENTS FOR USE BY THE COUNCIL

Having considered the rationale and risk associated with Non-Specified Investments, the following have been determined for the council's use:

	In-house use	**Maximum maturity**	**Max % of portfolio**	**Capital expenditure?**
▪ Deposits with banks and building societies over 1 year ▪ CDs with banks and building societies	✓ ✓	5 years	25% in aggregate	No
▪ Term deposits with other UK local authorities	✓	10 years	25% in aggregate	No
▪ Gilts ▪ Bonds issued by multilateral development banks ▪ Bonds issued by financial institutions guaranteed by the UK government ▪ Sterling denominated bonds by non-UK sovereign governments	✓ (on advice from treasury advisor)	10 years	20% in aggregate	No
Money Market Funds and Collective Investment Schemes, which are not credit rated	✓ (on advice from treasury advisor)	These funds do not have a defined maturity date	20%	No
Corporate Bonds	✓	5 years	20%	Yes (currently); No (from 01/04/12 provided legislation is adopted as anticipated)
Collective Investment Schemes (Pooled funds) which do not meet the definition of collective investment schemes in SI 2004 No 534 or SI 2007 No 573	✓ (on advice from treasury advisor)	N/a – No defined maturity date	£2million	Yes

In determining the period to maturity of an investment, the investment should be regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty.

APPENDIX 6

TREASURY MANAGEMENT POLICY STATEMENT

1. Statement of Purpose

1.1 Herefordshire council adopts the recommendations made in CIPFA's *Treasury Management in the Public Services: Code of Practice,* which was revised in 2011. In particular, the council adopts the following key principles and clauses.

2. Key Principles

2.1 Herefordshire council adopts the following three key principles (identified in Section 4 of the Code):

- The council will put in place formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of its treasury management activities.

- The council will ensure that its policies and practices make clear that the effective management and control of risk are prime objectives of its treasury management activities and that responsibility for these lies clearly with the council. In addition, the council's appetite for risk will form part of its annual strategy and will ensure that priority is given to security and liquidity when investing funds.

- The council acknowledges that the pursuit of best value in treasury management, and the use of suitable performance measures, are valid and important tools to employ in support of business and service objectives, whilst recognising that in balancing risk against return, the council is more concerned to avoid risks than to maximise returns.

3. Adopted Clauses

3.1 Herefordshire council formally adopts the following clauses (identified in Section 5 of the code):

- The council will create and maintain, as the cornerstones for effective treasury management:

  - A treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities;

  - Suitable treasury management practices (TMPs), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

  The content of the policy statement and TMPs will follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of the council. Such amendments will not result in the organisation materially deviating from the Code's key principles.

- Full Council will receive reports on treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close.

- The responsibility for the implementation and regular monitoring of treasury management policies and practices is delegated to Cabinet and for the execution and administration of treasury management decisions to the Chief Officer-Finance and Commercial, who will act in accordance with the organisation's policy statement and TMPs and, if he or she is a CIPFA member, CIPFA's Standard of Professional Practice on Treasury Management.

- Overview and Scrutiny Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

4. Definition of Treasury Management

4.1 Herefordshire council defines its treasury management activities as: -

'The management of the organisation's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.'

5. Policy Objectives

5.1 Herefordshire council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the council, and any financial instruments entered into to manage these risks.

5.2 Herefordshire council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

FINANCIAL RESOURCE MODEL 2012-15

MTFRM	**2011/2012 Budget £'000**	**2012/2013 Budget £'000**	**2013/2014 Budget £'000**	**2014/2015 Budget £'000**	**2015/2016 Budget £,000**
Base Budget	**142,844**	**146,314**	**143,359**	**144,095**	**144,969**
Total Inflation	**2,962**	**2,345**	**2,913**	**3,002**	**3,098**
Inflated base budget	**145,806**	**148,659**	**146,272**	**147,097**	**148,067**
- Grants Rolled into Formula Grant (reduced figure)	10,832	(932)	(187)		
- Personal Social Services	1,961	1,480	259		
MTFMS Changes					
- Waste management - PFI Contract	0	0	500	500	500
- Whitecross PFI requirement	0	75	75	75	75
- Local Development Framework	(275)	300	(300)		
Shared Services					
- Revenue Costs	(204)	56			
- Capital Financing	292	8	0		
- Core team costs (rev)	9	(479)			
- Core team costs (capital financing)	(6)	(6)	42		
- Shared Services	250	100	0		
Capital Financing Costs					
- Cost of borrowing	570	(799)	(726)	145	(838)
- New capital funding	0	234	710	729	227
- Investment Income	0	(103)	(156)	(78)	(98)
Emerging Pressures					
- Student Finance	(70)	0	0		
- Income shortfall (car parking, land charges etc)	0	(75)	(112)	(113)	
- Management change reserve	500	0	(500)		
- Winter maintenance	(500)	0	0		
- Statutory changes creating pressures	1,029	544	0		
- Base budget funding issues	130	907	0		
- Other service pressures	650	785	0		
- Academy schools	(300)	(150)	(100)		
- West Midlands Councils	209	(209)	0		
- Retail Quarter Timescales	230	0	0		
- Relief road feasibility study		300	(300)		
Efficiencies & Savings					
- Directorate reductions	(4,594)	(9,288)	0		
- Contingency re timing of delivery of savings	313	177	0		

MTFRM	2011/2012 Budget £'000	2012/2013 Budget £'000	2013/2014 Budget £'000	2014/2015 Budget £'000	2015/2016 Budget £,000
Rising to the Challenge					
- Delayering Savings	(3,148)	0	0		
- Reducing the Pay Bill	0	0	0		
- Shared Services	(2,560)	(571)	(340)	0	0
New Homes Bonus	(660)	(754)	(800)	(800)	(800)
Council Tax Freeze Grant 2011/12 to 2014/15	(2,150)				
Move to show as part of Formula Grant		2,150			
Council Tax Freeze Grant 2012/13 only		(2,164)	2,164		
Use Freeze Grant for "Transformational Change"		2,164	(2,164)		
Top up contingency/insurance reserves		450	(450)		
General reserves	**(1,000)**	**0**	**0**		
Movement from Reserves	**(1,000)**	**500**	**0**		
Capacity to achieve desired Tax increase	**0**	**0**	**208**	**(2,586)**	**(2,884)**
TOTAL BUDGET	**146,314**	**143,359**	**144,095**	**144,969**	**144,249**
Council Tax increase	0.00%	0.00%	2.50%	2.50%	2.50%
<u>Assumptions</u>					
Assumed Pay and Price Increase					
Employees	0.00%	0.00%	1.0%	1.0%	1.0%
Employers pension contributions - additional on basic pay	0.7%	0.7%	0.7%	0.8%	0.9%
Other costs	2.0%	2.0%	2.0%	2.0%	2.0%
Income **C & CR only**	2.0%	2.0%	2.0%	2.0%	2.0%
Prov Formula Grant increase on previous year	-13.30%	-8.60%	-2.60%	-2.60%	-2.60%
Assumed Taxbase Increase	1.01%	0.72%	0.50%	0.50%	0.50%