

MEETING:	OVERVIEW AND SCRUTINY COMMITTEE
DATE:	14 JANUARY 2011
TITLE OF REPORT:	MEDIUM TERM FINANCIAL STRATEGY 2011/14 AND BUDGET UPDATE 2011/12
REPORT BY:	DAVID POWELL, DIRECTOR OF RESOURCES

CLASSIFICATION: Open

Wards Affected

County-wide

Purpose

To seek Overview and Scrutiny Committee's views on the draft Medium Term Financial Strategy (MTFS) for 2011/14.

The Committee's views will be considered by Cabinet on 20th January 2011, when they will make recommendations to Council on 5th February 2011 about the budget, including the level of Council Tax for 2011/12 and the Medium Term Financial Strategy for 2011/12 to 2013/14.

Recommendation(s)

That Overview and Scrutiny Committee comments on the contents of the MTFS including the approach to budget setting, so that Cabinet is informed of its views.

Key Points Summary

- The Council will set its Council Tax on 4th March 2011 based on a balanced budget. It cannot budget for a deficit.
- The analysis of the provisional local government settlement has confirmed a number of grants have ceased, others have reduced and are now part of the "general" Formula Grant.
- Herefordshire has been adversely affected by funding formula changes that remove £2.7m of funding.
- The 2011/12 net Budget total is £148.28m.
- A Star Chamber process has been used by JMT to identify and challenge savings proposals and service pressures.
- The set of principles and priorities that came from discussions between Cabinet Members and

Non-Executive Directors have been used to assess all proposals and the resultant service changes.

Alternative Options

- 1 Joint Management Team (JMT) have approved a balanced budget for 2011/12 and this is summarised in the Financial Resource Model (FRM) in the attached MTFs. It incorporates inflation, service pressures and other spending requirements, the financing of which has been identified from within the Formula Grant, service efficiencies and council tax.

Reasons for Recommendations

- 2 The proposed MTFs, shown in Appendix A, provides a financial planning framework for the next three years.

Introduction and Background

- 4 On 20th January 2011, Cabinet is requested to consider the budget proposals set out in the MTFs, in order to make a recommendation to Council for setting the 2011/12 revenue budget based on holding Council Tax at current levels.
- 5 The provisional Local Government Settlement was announced on 13th December 2010; the key components were:
 - The Formula Grant, which includes Revenue Support Grant and Redistributed Business Rates, is set at £60.125m. It is unlikely there will be changes to this figure when the final settlement is published in late January 2011.
 - Indicative figures have been provided for 2012/13. This confirms a continuing tightening financial picture for local government.
- 6 The Department for Education has yet to provide an overall Dedicated Schools Grant (DSG) estimate for 2011/12. However, we know that per pupil funding will be £4,723.65 per pupil. The planning total being used by the Council is 22,467 pupils..

Comprehensive Spending Review (CSR10)

- 7 CSR10 announced on 20th October 2010 was largely in line with the anticipated position and this in turn influenced the provisional Local Government Settlement announced on 13th December 2010. In summary CSR10 meant the following for Herefordshire:
 - If local authorities wish to take part in the voluntary scheme, Council Tax in 2011/12 will 'have the tax base funded at a rate of 2.5% in each year of CSR10'.
 - By 2014/15, £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; in 2011/12 the addition is £530m. In 2011/12 this is an additional £1.96m for Herefordshire and a further £1.48m in 2012/13.
 - £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. For Herefordshire this is £2.368m.
 - All ring fencing on grants will be removed, apart from a total of nine grants including the Dedicated Schools Grant and a new grant for public health, to be introduced in 2013. For Herefordshire this means we will have only six specific grants.

- The schools budget for 5 to 16 year olds will increase by 0.1% in real terms each year of the Spending Review period; this includes £2.5bn of funding for the new pupil premium.
 - The number of transport grants to councils is to be reduced; however, councils will gain greater control and flexibility over spending these grants.
 - Bus Operators' Subsidy will be reduced by 20%, but the statutory concessionary travel entitlements remain in place.
 - The 'New Homes Bonus' will be introduced to 'reward' councils granting planning permission for the construction of new homes, by matching Council Tax receipts for each new home built for a number of years, with an additional premium added. It is estimated that this will provide £660k per annum.
 - The Regional Growth Fund totals over £1.4bn over three years. A panel will assess funding bids from Local Enterprise Partnerships as well as the private sector.
 - Revenue grants to local authorities from DfT will be reduced by 28%.
 - From April 2011 grants currently paid outside Formula Grant worth more than £4bn, will be rolled into Formula Grant. For Herefordshire this is an estimated £13.55m.
 - From 2013/14 Council Tax Benefit (CTB) will be localised. We await details of this change.
- 8 A significant factor that added to the pressure faced in 2011/12 is the front loading of funding reductions. The profile of reduction is therefore uneven and for Herefordshire is 13.3%, 8.6% and 1.9% for the next three years.

Budget and Policy Process

- 9 The council has been preparing for the funding reduction for some time. In late 2009 there was evidence that the public finances would be reduced to meet the growing national deficit. As a result the process of preparing for the 2011/12 budget commenced as part of setting the current year's (2010/11) budget. In 2009 Directorates were asked to submit proposals for an anticipated 5% year on year reduction as part of the overall resource allocation framework. This approach used an estimated 15% reduction in government funding over three years that represented a best estimate in 2009 of an approach to address the national deficit. These figures were built into the 2010 Medium Term Financial Strategy (MTFS) agreed by full Council in March 2010.
- 10 A series of meetings (Star Chambers) have been held by JMT in preparation for the anticipated financial pressures ahead where Directors were challenged by the Chief Executive, Deputy Chief Executive and Director of Resources about savings targets and financial pressures. Over the same period, Cabinet has met informally to consider the emerging picture. Joint meetings have also been held with the Non-Executive Directors of NHS to consider the impact across HPS. These preparations were focussed on the anticipated dates of Government announcements.
- 11 The provisional Local Government Settlement was announced on 13th December 2010. This was one of the latest announcements in recent times. The settlement includes a reduction in formula grant funding of £11.008m when comparing a rebased 2010/11 funding position with 2011/12. After taking into account further reductions and allowing for additional allocations of social care funding there is a net funding loss of £11.206m in 2011/12.
- 12 At Joint Management Team on 4th January 2011 options to close the position were discussed including the outcomes of the Star Chambers to date. A number of possible measures were reviewed.

- 13 It is proposed that the 2011/12 budget will also include the setting up of a budget management reserve to be held on the balance sheet. In addition the general fund reserve will remain at the policy - a minimum of 3% of net budget. This means that the general fund reserve will be £4.5m in 2011/12.

Star Chambers

- 14 The overall budget and policy process is now concluding. The Star Chambers had four key aims:
- To sign off the ongoing 5% savings previously identified for 2010 and beyond.
 - To review future savings identified in Star Chambers earlier in 2010.
 - To identify further cross cutting savings from the 'Rising to the Challenge' transformation programme and challenge existing proposals. These are primarily Streamlining the Business (shared services, organisational redesign, office accommodation and commercial strategy), People & Performance (reducing the pay bill, agency spend), Communities First (property review) and Customer Services (replacement CRM).
 - To challenge and review all submitted service pressures.
- 15 In order to guide those attending star chambers in the search for further savings and the necessary service changes, Joint Management Team (JMT) agreed core principles and priorities on 12th October. These re-emphasised the need to bring policy based issues to the centre of the process. Given the financial challenge ahead, the following core principles for the future were agreed.

PRINCIPLE	IMPACT
Valued Services	<ul style="list-style-type: none"> • Focusing on what matters to people, core business, stopping things we don't need to do
Cutting Red Tape	<ul style="list-style-type: none"> • Less regulation and bureaucracy, smaller local government
Supporting the Vulnerable	<ul style="list-style-type: none"> • Targeting more resources on individuals, families, communities at risk or disadvantaged; early intervention/prevention
Cutting Costs	<ul style="list-style-type: none"> • Reducing the pay bill; third party spend savings; smarter delivery
Local Delivery	<ul style="list-style-type: none"> • Devolution, role of parishes and the VCS; working through the nine localities
Personal Responsibility	<ul style="list-style-type: none"> • Self reliance, people and communities helping themselves, behavioural change

Alongside these principles the priorities to be delivered in the medium term were expressed in the form of the Joint Corporate Plan which is still being revised and is due to be considered by Cabinet on 20th January 2011.

PRIORITY	IMPACT
A resilient Herefordshire	<ul style="list-style-type: none"> • Preserving our environment and access to the countryside • Promoting access to services in rural areas • Strong voice in the region
Creating a strong economy	<ul style="list-style-type: none"> • Regeneration of Hereford; delivery of ESG • Delivery of key infrastructure for growth • Small business growth: jobs and wages; broadband
Raising Standards for Children & Young people	<ul style="list-style-type: none"> • An affordable education system • Meeting safeguarding standards • Increasing primary school and pupil performance
Improving Health Care and Social Care	<ul style="list-style-type: none"> • Reforming care for Older People • Creation of the ICO: April 2011 • Planning for GP Consortium and Health Promotion changes
Promoting self reliant local communities	<ul style="list-style-type: none"> • A balanced housing market • Reducing fear of crime • Encourage community and parish planning
Commissioning the right services	<ul style="list-style-type: none"> • Streamlining working practices • High levels of customers and citizen satisfaction • A High quality workforce

The Organisational Development project has identified the preferred future structure for each directorate and the Star Chambers have identified the financial challenges; the shape of the organisation for the future is beginning to emerge.

16 Given the provisional settlement only covers two years Joint Management Team conducted more detailed financial planning over the two year period based on the Joint Corporate Plan. The settlement announced on 13th December 2010 was worse in terms of total reduction and timing of the reductions and therefore required a further phase. This saw Directors work to a further set of principles to help refine the budget proposals. These principles are as follows:

- Grant reductions and grants that have ceased will not be funded. Their relationship to changes in national government policy will need to be determined and if the case cannot be made that funding delivers a policy requirement then the funding will not be back filled.
- Any growth requirement will need to be self funded by directorates.
- The additional sums provided for Adult Social Care as part of the settlement and also via Health will be added to the overall control total for Adult Services.
- There will not be any additional capital borrowing in 2011 apart from meeting agreed prior year decisions that still have a sound business case or where borrowing commitments cover projects already being delivered. Spend to save funding will be made available where a sound business case demonstrates a positive revenue contribution.

- Inflation at 2% will be applied to budgets. There is also an assumption that fees and charges will be raised by inflation and that any subsidy of services through under recovery of fees will end. A review of fees as part of the emerging income policy will need to be undertaken and future level of fees and charges will be adjusted to ensure we eliminate any subsidies.
- The savings put forward as part of the Star Chamber process are to be signed off and delivered. Directors were asked to revisit the explanation for any reductions put forward as part of the Star Chamber process so that any decision stands up to any challenge.
- Directors were required to review savings proposals identified for 2012/13 to assess if these can be brought forward.

Budget Setting Principles

- 17 The attached draft Medium Term Financial Strategy includes the Council's financial model. This indicates the amounts built in to meet unavoidable commitments. It also includes reductions to balance the budget. Key points included in the model are as follows;
- a. Inflation: The model includes net inflation of £2.962m. It assumes that inflation will be added to discretionary charges.

In previous years inflation has not been applied to budget as a proxy for efficiency. This approach has ceased and does not form part of the 2011/12 budget framework.
 - b. Additional funding for Adult Social Care: The council will passport to Adult Social Care the £1.96m for Adult Services included in the formula grant and the £2.368m of funding from the NHS included in the CSR10 announcement. In order to support the transformation of Adult Services £750k of funding will also go to Adult Services. This will enable a continuation of the activity funded by the 2010/11 social care reform grant that is now part of general funding in 2011/12.
 - c. Shared Services: Funding and savings associated with the Shared Services programme is included in the financial model.
 - d. Budget Management Reserve: The potential pressures associated with the reduction in funding will require adequate reserves. The budget will include a £500k contribution to a specific budget management reserve. This will be brought to a level of £1m by the addition of £500k following a review of existing specific reserves.
 - e. Change Management Reserve: In 2010/11 a reserve was established to support costs associated with staff reductions. In 2011/12 the annual budget will increase to £1m.
 - f. Use of Reserves: Changes to the local government funding formula remove £2.8m of funding in 2011/12. The main reduction affects concessionary fare funding. In 2010/11 gross expenditure on concessionary fares of £1.8m is projected. In order to support concessionary fares' funding it is proposed £1m is temporarily used from specific reserves to ease financial pressure. This demonstrates the benefits of financial planning over more than one year with the sum being repaid in 2012/13 and to be included in the budget for that year.
 - g. The council will take advantage of government funding up to 2.5% of council tax increase and this is included in our financial plan. For Herefordshire this is £2.15m;

- h. An additional 0.7% of pay is included for the outcome of the actuary's revaluation of the pension fund;
- i. The front loading of government funding reductions announced in CSR10 is now included in the financial plan.

Provisional Local Government Finance Settlement 2010

- 18 The provisional settlement was announced on 13th December 2010 and remains subject to consultation until the end of January 2011. As previously indicated CSR10 and the subsequent provisional settlement form part of the Government's deficit reduction plan. In year savings for 2010/11 have already been made.
- 19 The provisional settlement gives local government greater flexibility to take decisions locally. Restrictions have been lifted on how local government spends its money by removing "ring fences". The intention is 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.
- 20 The provisional settlement covers two years (unlike CSR10 that covers the next four years). The shorter time frame is because local government is expected to have a new funding distribution system from 2013. It is anticipated that consultation on changes will commence in 2011.
- 21 The number of specific grants has reduced dramatically. In 2011/12 Herefordshire will receive only six specific grants compared with approximately 70 it received in 2010/11. The majority of funding is now via the general Formula Grant and this has been subject to a significant reduction of £11.008m for 2011/12 when compared with a like for like 2010/11 total for Formula Grant (plus grants rolled into Formula Grant for 2010/11). In summary this is as follows:

	£'000
2010/11 Formula grant	57,583
Grants rolled into Formula Grant	13,550
TOTAL	71,133
2011/12 Formula Grant	60,155
TOTAL loss in Formula grant	11,008

- 22 In addition a number of grants have been reduced or have ceased and these total £2.566m. However, £2.368m in NHS funding transferred to the Council to provide support for Social Care. This gives an additional net reduction of £198k and therefore when added to the £1.008m reduction the overall net position is a loss of £11.206m in funding for 2011/12.
- 23 The Council will receive £1.961m as part of the national allocation for Personal Social Services but this is within the 2011/12 formula grant total of £60.155m.

- 24 As part of the Local Government Settlement, the government reviews the funding formula that distributes funding to local authorities. The provisional settlement indicates that the Council has been badly hit by changes to the formula. The net change in grant is £2.7m, with the main variation arising from changes to concessionary travel funding distribution.
- 25 The Concessionary Bus Travel Act 2007 transferred responsibility for the concessionary travel scheme from district level authorities to county level authorities. To achieve this transfer, the funding needed to be transferred. District Councils are funded from the lower tier funding calculations, and county councils are funded from the upper tier funding calculations. Therefore, funding needed to be transferred from the lower tier to the upper tier, and this was achieved as part of the local government finance settlement for 2011/12 announced on the 13th December. However, the element of concessionary travel funded by special grant was transferred in to formula grant from 2011/12 onwards.
- 26 The formula grant consultation launched in the summer of 2010 presented 40 options for the transfer, with losses ranging from £1.5m-£3.5m for Herefordshire, based on the 2010/11 settlement. Due to the inherent unfairness of the transfer for unitary authorities we worked with organisations such as SPARSE Rural, the SCT and the LGA to persuade the government of this view. Subsequently, a 41st option was considered, which ensured a zero loss for all unitary authorities. This option was not supported by Government.

Savings proposals

- 27 As described earlier Directors were asked to frame savings proposals within an agreed set of principles coming out of the joint Cabinet/NED meeting on 28th October. This places the proposals within a framework that helps us meet the challenges ahead. In summary the proposals can be analysed by directorate or principle. The following tables provide the summarised information by directorate.

	2011/12 £'000	2012/13 £'000	TOTAL £'000
Adult Services	2,649	2,383	5,032
CYPD	1,747	839	2,586
DCX	1,033	853	1,856
Public Health	297	278	575
Resources	576	338	882
Sustainable Communities	2,200	1,092	3,292
TOTAL	8,502	5,783	14,223

In addition the Commercial Strategy will deliver £1.8m of savings in 2011/12. This gives overall savings of £10.27m. The overall 2011/12 savings being built into the budget total £10,302m and can be analysed as follows:

	£'000

Shared Services including Commercial Strategy	2,560
Reductions in the pay bill	3,148
Directorate reductions	4,594
TOTAL	10,302

Financial Management

- 28 It is important that the Council has appropriate levels of reserves at a time of financial challenge. The current policy for the general fund reserve requires it to be 3% of net revenue budget. The total net budget for 2011/12 is £148.8m and will require a reserve of £4.5m. In addition our non schools specific reserves total £7.87m.
- 29 It is proposed that a specific financial reserve is established following a review of current specific reserves. The reserve will need to be £1m and any future use repaid as part of the budget process. In order to incentivise sound financial management the first call on “repayment” should be the directorate that has overspent in the previous year.
- 30 The report has indicated that changes to the funding formula have affected concessionary fares funding. After the application of a specific grant the net expenditure in 2010/11 is £1.1m.
- 31 The current specific grant is now part of formula grant and has also been reduced. For 2011/12 it is proposed that a sum of £550k is passported within formula grant and that temporary support of £1m is provided by temporary use of the current £2.774m Waste Reserve. The 2012/13 budget would require this to be repaid and the base budget would be adjusted.
- 32 The above will mean that £1.5m of funding for concessionary fares is available in 2011/12. A reduction in expenditure on concessionary travel will still be needed. This could be achieved by meeting guidance for availability of concessionary fares; this will yield approximately £200k of savings. The measures outlined will protect concessionary travel funding and provide £1.55m of funding compared with £1.8m in 2010/11.

Provisional 2012/13 Settlement

- 33 The two year settlement provisionally allocates £54.4m of formula grant to Herefordshire for 2012/13 with a new methodology to be in place for 2013/14. For this reason local authorities have a two year financial settlement compared with the four year timeframe of CSR10.

Legal Implications

- 34 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.

35 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

36 Clearly, there is the potential risk that the public finance will be in worse shape than assumed as part of CSR10. The appropriate management would be via further cost reduction.

37 The additional risk that may occur is if the services currently supported through former specific grants are no longer funded because of a change in priorities. This would need to be managed over time.

Appendices

Medium Term Financial Strategy 2011/14

Background Papers

- None identified