COLCHESTER

# Cabinet

**7 September 2016**

**Item 7(i)**

| | | | |
|---|---|---|---|
| **Report of** | **Assistant Chief Executive** | **Author** | **Sean Plummer** ☎ **282347** |
| **Title** | **2016/17 and 2017/18 Budget Update** | | |
| **Wards affected** | Not applicable | | |

**This report provides Cabinet with an update on the 2017/18 Revenue Budget forecast, Government funding issues and changes to the Council's treasury management strategy**

## 1. Decisions Required

1.1 Cabinet is requested to consider the following items:

i) Agree to reallocate funding as set out in paragraphs 5.3 and 5.4.

ii) Note the updated 2017/18 budget forecast as set out at paragraph 6.2 shows a current gap of £625k and that progress has been made to identify savings to assist with the delivery of the budget strategy.

iii) To agree to "apply to accept" the Government's 4 year funding settlement with the publication of a required efficiency statement delegated to Assistant Chief Executive in consultation with the Portfolio Holder for Resources.

iv) Note the assumption that the Essex business rates pool will continue in 2017/18 and that an updated position will be reported to the next Cabinet meeting.

v) To agree that the Assistant Chief Executive in consultation with the Portfolio Holder for Resources will reply to the Government consultation on 100% localisation of business rates.

vi) To agree the changes to the treasury management strategy sets out in section 8 including the change to the MRP policy.

## 2. Reasons for Decisions

2.1 The Council is required to approve a budget strategy and timetable in respect of the year 2017/18.

2.2. This report relates to the budget update, review of the current year's budget allocations, the Government's 4 year settlement offer and revisions to the treasury management strategy.

## 3. Alternative Options

3.1 There are different options that could be considered and as the budget progresses changes and further proposals will be made and considered by Cabinet and in turn Full Council.

3.2. The Council could choose not to accept the Government's 4 year settlement offer, however, this would not provide the certainty in respect of future funding and may result in lower grant funding in the coming three years.

## 4. Background

4.1 A timetable for the 2017/18 budget process (see Appendix A) was agreed at Cabinet on 13 July 2016.

4.2 At this stage in the budget process it is important to consider progress on the budget and any in year issues. Detailed budgets are currently being produced with the aim to complete this task by December. Work is currently progressing well and is in line with the budget timetable.

4.3 This report also includes an update on Government funding and arrangements in respect of business rates pooling and the consultation in respect of the proposal to localise 100% of business rate income.

4.4 The report also provides a review of changes proposed to the treasury management strategy.

## 5. Budget 2016/17 - Review

5.1. The Governance and Audit Committee will review the budget position for the current year including outturn projections on 13 September 2016. The total position reported, at what is an early stage, shows that the outturn is currently expected to be broadly in line with the budget.

5.2. Scrutiny Panel will receive a report on the half year position on 8 November 2016 and this will in turn be reported to Cabinet when any impact on balances will be assessed.

5.3. A review of allocations of one-off funding has been carried out to ensure that these are all still required and it is now proposed that the following sums could be reallocated to other projects:-

| Scheme | Funding Source | £'000 | Comments / Questions |
|---|---|---|---|
| Winter Wonderland | Borough Investment for All (BIFA) | 15 | Funding allocated not required. |
| Lighting the walls | Allocation from funding set aside for street lights. | 20 | Feasibility work has been undertaken into possible schemes and costs for lighting the Walls and Key Heritage Sites and the estimates range from £50,000 up to a total of £250,000. This project cannot proceed as such larger budgets would be required. |
| New Homes Bonus (NHB) Strategic Plan Priorities - Unallocated | NHB – 15/16 | 159 | £388k of the original budget of £547k has been allocated to various projects. The remaining balance of £159k is therefore available to support other projects and is included here. |
| | | **194** | |

5.4. Cabinet members have considered emerging issues for using this funding and it is proposed to allocate it to the following projects:-

| Proposal | Cost £'000 | Description / supporting information |
|---|---|---|
| Grant Funding allocation | 100 | A grant funding pot of £100k similar to the Big Choice scheme to enable Community Groups and Projects to do more in their local areas. The public will have a say in who gets the money again this year but the approach will include the opportunity to bid for smaller amounts of funding, opening up the grants to smaller organisations and aimed at those who may not usually apply for public funds. |
| Events | 40 | Allocation of £40k for a range of events and activities in or around the Town Centre over the next twelve to eighteen months aimed at increasing footfall and visitors alongside supporting the vibrancy and economy of the Town. |
| Rent deposit guarantee scheme | 30 | Establishment of a rent deposit scheme to be used to provide a rent deposit/advance for new private sector tenancies for around 25 families who present as homeless, and so reduce the use of temporary accommodation. Scheme to be administered via the Credit Union so it can be returned at the end of the tenancy and "re cycled" to benefit new families. |
| Establish funding for homeless families for new home start up. | 24 | Fund to support approximately 50 families who are rehoused as homeless and are having to establish a new home on very low levels of income. Fund will provide essential furnishing and appliances (e.g. cooker, fridge, bed) in partnership with Colchester furniture projects to reduce recourse to high-cost loans. |
| **Total** | **194** | |

## 6. Summary of 2017/18 Budget Forecast

6.1. Cabinet considered the 2017/18 budget position and strategy on 13 July 2016. At this stage a budget gap for 2017/18 of £766k was reported. The following sets out work under the way and one specific change to the forecast.

6.2. The following table shows the previous budget forecast and revised position which now shows a reduced budget gap of £625k

| | **Reported in July** | **Updated Position** |
|---|---|---|
| | **2017/18** | **2017/18** |
| | **£'000** | **£'000** |
| **Base Budget** | 23,959 | 23,959 |
| Adjustment for c/f items (one off items) | (111) | (111) |
| Cost Pressures (net of one off changes) | 956 | 956 |
| Growth Items (net of one off changes) | 156 | 15 |
| Savings | (1,300) | (1,300) |
| **Forecast Base Budget** | **23,660** | **23,519** |
| *Funded By:* | | |
| Revenue Support Grant | (920) | (920) |
| Business Rates Baseline | (4,038) | (4,038) |
| *Settlement funding* | *(4,958)* | *(4,958)* |
| Increase in NNDR / taxbase above baseline | (900) | (900) |
| New Homes Bonus | (5,754) | (5,754) |
| ***Total Gov't grants*** | ***(11,612)*** | ***(11,612)*** |
| Council Tax | (11,010) | (11,010) |
| Use of Reserves | (272) | (272) |
| **Total Funding** | **(22,894)** | **(22,894)** |
| **Budget gap** | **766** | **625** |

6.3. The change relates to the removal of £141k growth item in respect of the food waste service. The cost of the food waste service has been funded from a specific Government and the pressure reflected the residual cost as the grant is all used. We expect there to be sufficient grant to fund the cost of the food waste service in 2017/18 and therefore the budget pressure has been removed.

6.4. In the last two years reviews of the outturn position have been carried out to identify where budgets should be adjusted to reflect where they are not fully spent, or where we receive more income. A further outturn review has been carried out as part of the 17/18 budget strategy and includes consideration of some income budgets such as planning and car parking where income has exceeded budgeted sums. Details of this will review be presented to Cabinet later in the year but it is expected that this will provide the opportunity to reduce the budget gap.

6.5. Further items that are currently being reviewed include:-

*Local Authority Carbon Management – energy savings*

6.6. The Council agreed funding for a number of projects and these are expected to deliver costs savings. These will be reviewed alongside energy budgets in October when new energy prices will be confirmed.

*Interest Budget*

6.7. Changes to the Council's treasury management strategy are set out later in this report. There are a number of potential budgetary implications relating to the Council's treasury management activities including:-

- a reduction in investment income following the change in Bank Rate from 0.5% to 0.25%.
- any cost arising from any new borrowing
- any additional borrowing cost arising from capital programme funding such as the Northern Gateway North sports hub proposals considered by Cabinet in March 2016.
- The revenue impact of changes to the Minimum Revenue Provision referred to later in this report.

6.8. Currently no provision is included in the budget forecast for costs or savings related to these factors and this will need to be assessed in future budget updates.

## 7. Government Grants / Funding

7.1. The 2016/17 Finance Settlement included the announcement of an "offer" of a four year funding settlement. The key points to note are:-

- In return for accepting the offer councils are required to publish an "efficiency plan"
- There will still be an annual settlement which will include changes to take account of final business rate multipliers.
- There may also be changes such as transfer of functions to or between local authorities or any unforeseen events.

7.2. Councils have until 14th October 2016 to decide whether to "apply to accept" this offer. No real guidance has been provided on what should be included in the efficiency plan, explaining that it should be locally owned and locally driven. It has to cover the four year period and be "open and transparent about the benefits" this will bring to the Council and community. A copy of the letter from the then Secretary of State is available as a background paper

7.3. The 4 year settlement includes 3 grants as shown below:-

| | 16/17 | 17/18 | 18/19 | 19/20 |
|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 |
| Revenue Support Grant (RSG) | 1,978 | 920 | 275 | (446) |
| Transition grant | 88 | 87 | - | - |
| Rural Services grant | - | - | - | - |
| **Total** | **2,066** | **1,007** | **275** | **(446)** |
| *Cumulative reduction over period* | | *1,059* | *1,791* | *2,512* |

7.4. In 2019/20 the 4 year settlement indicates that Colchester will pay the Government £446k via an increased business rate "tariff" payment.

7.5. As 2016/17 grant figures are already being paid the offer only really relates to 2017/18 and 2018/19 and the *negative* RSG in 2019/20. In total these changes amount to a reduction in grant of £2.5million in the next three years.

7.6. Following correspondence with a Government representative they have confirmed that:-

- the offer includes the negative RSG and they responded as follows
- this is a minimum offer that the Government intend to build on over the course of the parliament and that nobody will ever be worse off for accepting the offer.
- There are still a significant number of decisions to make ahead of 19/20, particularly on the introduction of 100% business rates retention and the fair funding review. Both are out for consultation/discussion at the moment and will be worked up with the sector so we cannot predict the outcome.

7.7. The Local Government Association (LGA) has summarised the offer as follows:-

| Upside | Downside |
|---|---|
| • A step in the direction of what we have been asking for.<br>• An incentive to plan longer term and drive through risky change<br>• A 'nudge' towards best practice<br>• An opportunity to take greater risk | • The amount guaranteed is really quite small for many councils.<br>• Year 5 is probably the most uncertain |

*The Efficiency Plan*

7.8. As stated no real formal guidance exists on what this should include. Appendix B sets out a draft summary of the main areas that will be included in the plan. This reflects some advice from CIPFA / LGA and the general intention is that it tries to bring together information in existing plans and policies. It is proposed that the publication of the final document is delegated to the Assistant Chief Executive in consultation with the Portfolio Holder for Resources.

**New Homes Bonus**

7.9. The Government's consultation on "sharpening the incentive" of the New Homes Bonus closed on 10 March 2016. To date the Government has not issued any response to the consultation and therefore the level of grant for 2017/18 remains uncertain.

**Business Rates**

7.10. There are two specific issues in respect of business rates to consider in this report.

*Business Rates Pooling*

7.11. For 2015/16 and 2016/17 the Council has been part of an Essex business rate "pool". The rationale for this is that the pool provides an opportunity to keep a greater share of NNDR income above the baseline. Based on figures provided as part of the 2015/16 closure of accounts there is an estimated gain of £0.2m, however, this is subject to change and final business rates figures which will be finalised for all pool members by October. The estimated £0.2million additional income kept in Colchester is as a result of the decision to join the Essex pool. This money would otherwise have been paid over to Government.

7.12. It is too early to estimate any additional income that we might achieve from the pool arrangement in 2016/17; any such gain would not be known until 2017/18. It is unlikely that we will be able to estimate this as part of the 2017/18 budget setting process as it not only relates to our own figures which are subject to a degree of risk and variation but also figures of partner authorities in the pool.

7.13. No guidance has been issued by Government yet on business rates pooling in 2017/18 and therefore the assumption is that existing arrangements will remain unchanged.

7.14. The Essex pool agreement stays in place for 2017/18 unless there are new members who wish to join the pool or there are any existing pool members who wish to leave the pool. In either case, under existing arrangements it will be necessary to make a new submission to Government by 31st October to express an interest in creating a 'new' pool.

7.15. Pool members and other Essex authorities are currently considering their position and a further update will be reported to Cabinet in October.

*Business Rates Consultation*

7.16. Department for Communities and Local Government's consultation on 'Self-sufficient local government: 100% Business Rates Retention', was published in July. Alongside this consultation a discussion paper on 'Fair Funding Review: Call for evidence on Needs and Redistribution' was published. Both documents are available here: https://www.gov.uk/government/consultations/self-sufficient-local-government-100-business-rates-retention.

7.17. The proposals in the consultation set out that by the end of this Parliament, local government will retain 100 per cent of taxes raised locally. In order to ensure that the reforms are fiscally neutral, councils will gain new responsibilities, and some Whitehall grants will be phased out.

7.18. To achieve such radical reform, the Government wants councils, business and people to take the initiative and shape the design of the new system. This consultation is therefore deliberately open and seeks views and ideas across all aspects of the reforms.

7.19. It identifies some of the issues that the Government thinks should be kept in mind in designing of the reforms. This includes how the reformed system recognises the diversity of different areas and the changing pattern of local governance arrangements. The system need not work in the same way across the country.

7.20. It also considers how the design of the new system can provide the right level of incentive and reward to those councils (particularly those working closely with local businesses and together as Combined Authorities) that pursue policies that drive additional growth in their areas.

7.21. It also welcomes views on how business rates income might be shared across different tiers of local government, including how the system should recognise areas which have moved to reformed models of governance. There is a balance to be struck between providing a strong incentive for growth in local areas and considering the distribution of funding between local authorities.

7.22. The Government is clear that the reformed system should ensure that authorities are able to manage and share risk to an acceptable level, and that they are insulated from undue shocks or significant reductions in their income.

7.23. The deadline for responses is 26 September 2016 and consideration is being given an Essex wide response.

7.24. It is recommended that a reply on behalf of this Council is delegated to the Assistant Chief Executive, in consultation with the Portfolio Holder for Resources.

## 8 Treasury Management Strategy

8.1. This report proposes a number of changes to the 2016/17 Treasury Management Strategy Statement (TMSS) that was approved by Council on 17 February 2016. These changes are as a result of changes to borrowing rates, credit ratings and interest rate forecasts following the outcome of the EU referendum on 23 June 2016, which includes the Monetary Policy Committee cutting the bank rate from 0.50% to 0.25% on 4 August. They are as follows:

### Interest rate forecast

8.2. The table below compares our treasury adviser's latest interest rate forecasts with those that were included in the TMSS. Economic forecasting remains difficult, however the overall longer run trend is for rates to rise gently, albeit with the overall balance of risks remaining to the downside.

| | | Q3 2016 | Q1 2017 | Q1 2018 | Q1 2019 |
|---|---|---|---|---|---|
| Bank Rate | TMSS | 0.75% | 1.00% | 1.75% | 2.00% |
| | Now | 0.25% | 0.10% | 0.10% | 0.25% |
| PWLB 5 year | TMSS | 2.70% | 2.80% | 3.30% | 3.60% |
| | Now | 1.00% | 1.00% | 1.10% | 1.20% |
| PWLB 10 year | TMSS | 3.20% | 3.40% | 3.80% | 4.10% |
| | Now | 1.50% | 1.50% | 1.60% | 1.70% |
| PWLB 25 year | TMSS | 3.90% | 4.10% | 4.30% | 4.50% |
| | Now | 2.30% | 2.30% | 2.40% | 2.50% |
| PWLB 50 year | TMSS | 3.80% | 4.00% | 4.20% | 4.40% |
| | Now | 2.10% | 2.10% | 2.20% | 2.30% |

8.3. Our treasury adviser's latest advice is that as yields are at historic lows borrowing should be considered if appropriate to the strategy. As the outlook is uncertain, it is suggested that any borrowing is taken in tranches so as to benefit from the current rates, but also provide some flexibility if rates fall further.

### Borrowing Strategy

8.4. The TMSS states that the Council is currently maintaining an under-borrowed position. This means that the capital borrowing need has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is relatively high. This means that there would be a cost of carry to any new borrowing which causes an increase in investments, as this will incur a revenue loss between borrowing costs and investment returns.

8.5. At 31 March 2016 the Council's Capital Financing Requirement was £153.5m and, net of finance lease liabilities, the underlying borrowing requirement was £150.3m. The Council's external borrowing totalled £136.1m, which meant under-borrowing was £14.2m, of which £3.4m relates to the HRA. This means that the Council could borrow £14.2m in respect of its current borrowing need.

8.6. On the basis of the above forecasts, if the Council borrowed to its current CFR for 50 years (2.10%), the annual interest cost would be £300k. This would be mitigated by around £36k if this were invested for the duration of the year (based on the latest budgeted investment rate of 0.25%), meaning that the annual cost of carry would be £264k. This is not currently budgeted for, so should be considered as a potential cost pressure.

8.7. Against the above, the long term saving resulting from borrowing at very low rates should be considered. Assuming current rates increase in accordance with the above forecast, the annual interest cost would only increase by £27k p.a. if borrowing were delayed until the beginning of 2019. However, this would lead to the cost of borrowing being significantly higher over the life of a 50 year loan.

**Investments - Country Limits**

8.8. The TMSS states that the Council will only use approved counterparties from countries with a minimum sovereign credit rating of AA-, based on the lowest available rating. Subsequent to the EU referendum decision, the following action has been taken by the ratings agencies regarding the UK sovereign rating:

*Fitch*

- Sovereign rating downgraded by one notch, from AA+ to AA.
- Outlook lowered to Negative, from Stable.

*Moody's*

- Sovereign rating affirmed, at Aa1 (equivalent to AA+ from Fitch / S&P).
- Outlook lowered to Negative, from Stable.

*Standard & Poor's (S&P)*

- Sovereign rating downgraded by two notches, from AAA to AA.
- Remains on Negative Outlook.

8.9. It is proposed that whilst our minimum sovereign debt limit is now in line with Capita's recommendation, this section should be amended to state that this policy excludes the UK. This will take account of any further deterioration in the UK's credit rating.

**Investment Strategy**

8.10. The Investment Strategy in the TMSS assumed that the Bank Rate would remain unchanged at 0.5% before starting to rise from quarter 2 of 2016. On this basis the suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during the year was 0.90%.

8.11. The current forecast suggests that budgeted investment earnings for 2016/17 should be amended to 0.25%. This is likely to have an adverse impact on the Central Loans and Investment Account.

**LOBO Loans**

8.12. Unrelated to the referendum vote, Barclays Bank contacted the Council on 20 June 2016 to state that they had decided to waive their right to change the applicable interest rate of the Council's two Lender Option/Borrower Option (LOBO) loans in the future. As a result the two loans, which total £9 million, effectively become fixed rate loans at their current investment rates with their stated maturities.

8.13. The Council's LOBO loans are subject to six monthly calls, and the maturity profile is shown as the next call date, and as such they are accounted for as short-term loans. The financial impact of the change is that these loans will in future periods be shown as long-term market debt, which will have an impact on prudential indicators relating to the maturity profile of debt.

**Minimum Revenue Provision (MRP) Policy**

8.14. For capital expenditure incurred before 1 April 2008, the MRP policy currently follows the existing practice outlined in former CLG regulations, which provides for an approximate 4% reduction in the borrowing need (CFR) each year on a reducing balance basis.

8.15. It is now the view of the Council's external Auditors (Ernst & Young) that there is no obligation to repay on this basis. Instead this historic element of MRP can now be paid on an equal instalment basis over a period of 50 years. This change would have the benefits of reducing the amount payable by the Council over the next 17 years, introducing a consistent level of charge, and ensuring that this element is eventually completely repaid.

8.16. In 16/17 this change of approach would reduce this element of the MRP charge from £186,684 to a standard amount of £93,342.

## 9. Proposals

9.1 It is proposed that:-

- The funding shown in paragraph 5.3. be reallocated to the schemes shown at paragraph 5.4.
- Note the updated budget forecast for 2017/18 and commentary on work in progress.
- To agree to "apply to accept" the Government's 4 year settlement and delegate the approval of the required efficiency statement to the Assistant Chief Executive in consultation with the Portfolio Holder for Resources.
- To note that it is assumed that the Essex Business Rates Pool will continue in 2017/18 and that an update will be reported to the next Cabinet meeting.
- To note the Government's business rates consultation and that a response will be made by the Assistant Chief Executive in consultation with the Portfolio Holder for Resources.

- To agree the changes in the treasury management strategy set out in section 8 including the MRP policy.

## 10. Strategic Plan References

10.1. The 2017/18 budget and the Medium Term Financial Forecast will be underpinned by the Strategic Plan priorities and will seek to preserve and shift resources where needed to these priorities.

## 11. Consultation

11.1. The Council is required to consult on its budget proposals. A consultation exercise took place as part of the production of the Strategic Plan agreed by Council in February 2015.

11.2. The budget strategy and timetable aims to ensure that information is available for scrutiny and input from all Members on proposals in the process. The aim is that detailed information will be available prior to the final budget report being submitted to Cabinet and approval by Council in February.

11.3. As has been the case in previous years the opportunity remains open for the leader of the opposition to meet with officers to assist with consideration of any alternative budget proposals.

11.4. Furthermore, we will continue with the statutory consultation with business ratepayers and will meet with parish councils in respect of grant funding.

## 12. Financial implications

12.1 As set out in the report

## 13. Equality and Diversity Implications

13.1 Consideration will be given to equality and diversity issues in respect of budget changes proposed as part of the budget process. This will be done in line with agreed polices and procedures including production of Equality Impact Assessments where appropriate.

## 14. Risk Management Implications

14.1. The strategic risks of the authority will be considered in developing the 2017/18 budget and all forecast savings/new income options will be risk assessed as part of the budget process. This report sets out some of the key risks / variables at this stage in the budget process and as stated earlier this will be refined during the year.

## 15. Other Standard References

15.1 There are no specific Publicity, Human Rights, Community Safety or Health and Safety implications at this stage.

**Background Papers**
Report to Cabinet 17 July 2016
Letter from Secretary of State in respect of 4 Year Settlement

**Appendix A**

| **2017/18 Budget Timetable** | |
|---|---|
| **Budget Strategy** | |
| **March – June (SMT and Budget Group)** | Budget Group Meetings Agreed<br>Update MTFF /Budget Strategy<br>Review potential cost pressures, growth and risks<br>Consider approach to budget<br>Initial budget reviews started |
| **Cabinet – 13 July 16** | • Review 15/16 outturn<br>• Report on updated budget strategy / MTFF<br>• Timetable approved |
| **Scrutiny Panel – 19 July 16** | Review Cabinet report |
| | |
| **Detailed Budget preparation and Budget Setting Consultation** | |
| **Budget Group / Leadership Team regular sessions on progress / budget options now - December** | Review budget tasks<br>Consider delivery of existing budget savings<br>Complete outturn review |
| **Cabinet – 7 September 16 and /or 12 October 16** | • Budget Update<br>• Consider “4 year settlement”<br>• Review of capital resources / programme |
| **Cabinet – 30 November 16** | • Budget update<br>• Reserves and balances<br>• Agree fees and charges / budget changes<br>• Government Finance settlement (if available)<br>• Review in year budget position |
| **Scrutiny Panel – 31 January 17** | Budget position (Detailed proposals) |
| **Cabinet – 1 February 17** | Revenue and Capital budgets recommended to Council |
| **Council – 22 February 17** | Budget agreed / capital programme agreed / Council Tax set |

*Leadership Team to review budget progress during year.*

Appendix B

**Draft Outline Efficiency Plan**

**Introduction / Background**
Headlines on the Council's performance in recent years on delivering savings / income.
Comment from auditors on value for money opinion.
Links to Council's Strategic Plan

**The budget position / MTFF**
Summary of current MTFF

**The approach to manging budgets gaps and deliver a balanced budget**
Include savings / income built into plans:-

- Digital challenge (including partnership working)
- Commercial income / savings (role of the Revolving Investment Fund)

Approach to closing remaining budget gaps:-

- Outturn review
- Targeted budget reviews
- Carbon management
- Other partnerships / joint working opportunities & other commercial opportunities
- Business rate assumptions
- Housing development

The above will touch on themes of:-

- Demand management / how customers contact us
- Delivering new / more income through commercial activities
- Delivering economic growth through RIF projects

**Risks and reserves**
Comments on key risks / reserves / balances

**Links to other documents**
Strategic Plan
HRA
Statement of Accounts