Agenda Item: 5(G)

BUSINESS SUPPORT
OVERVIEW AND SCRUTINY COMMITTEE

15 OCTOBER 2009

MEDIUM TERM FINANCIAL PLAN 2010/2013

Report from: Mick Hayward, Chief Finance Officer

Author: Mick Hayward, Chief Finance Officer

Summary

This report reviews the major financial issues facing the Council in this and the next three years. It also provides a framework for the more detailed preparation of the draft Revenue Budget for 2010/2013.

1. Budget and Policy Framework

1.1 The council's annual budget and council tax setting establishes the council's budget framework, and sets out the funding of services. The Medium Term Financial Plan identifies the key issues that need to be addressed as part of that budget preparation. This Medium Term Financial Plan will mesh with the review of the Council Plan in preparing the Corporate Plan for 2010/13. This will seek to integrate budget setting with service planning and ensure priorities and funding are matched.

2. Background

2.1 For the past few years the Council's budget has been prepared against a backdrop of a serious deficit in resources and inevitably the focus has been on achieving the necessary balance for the immediately forthcoming year and there has been much less, if any, focus on the future. This is despite a succession of Medium Term Financial Plans prophesying the very deficits that manifest, usually to a greater degree, when the detail of budget preparation begins to become apparent.

2.2 However, against this, it needs to be recognised that the budgets we have set, certainly for 2008/09 and the current year, have probably been the most robust and least prone to financial risk that Medway has ever had. Indeed the 2008/09 outturn was an unprecedented level of underspending and the current budget monitoring points to an underspend this year on General Fund services. There is a danger that this has the unfortunate side effect of inspiring a belief that all is well with the Council's finances and whilst the processes for setting and managing budgets are robust, it is common knowledge that the public sector in general will be severely challenged in terms of resources in the coming years as a consequence of actions necessary to mitigate the worldwide financial crisis and recession of the past year.

2.3 It is acknowledged that Medway has a low resource base both in terms of per capita grant and council tax. For the Dedicated Schools Grant (DSG) the position is somewhat better with Medway above funding levels for statistical neighbours and only marginally below the national average, but of course these funds are passported through to schools based activity with a restricted proportion available to support centrally retained activities that have themselves been under significant pressure in recent years.

2.4 It is also clear, even at this early stage, that the future budget requirement, incorporating investment in meeting strategic objectives allied with regulatory change inspired by the likes of the Laming review, will exceed available resources. There have been a number of dire scenarios predicted about resource levels for 2011/12 and beyond but whatever the outcome of that debate Government have already declared a target of 4% cash releasing savings for next year which equates to some £8 million and it may well be that future years targets are higher still. It will be necessary at the very least to identify areas where efficiency savings can be made and/or more radical changes to services can be effected, to enable the Council to deliver affordable services and maintain a momentum of delivering improved services that cost less.

3. Advice and analysis

3.1 The world wide economic recession and the massive growth in public sector borrowing in the UK in particular, will have an inescapable effect upon present and future public sector finance. It is a fact that regardless of the political colour of the Government, there will have to be a retrenchment from the scale of growth the public sector and the NHS and Local Government in particular, have enjoyed in recent times. This year’s increase in Formula Grant was 4.03% and for 2010/11, the third and final year of the current spending review, the announced provisional increase is 3.6%. There is no intelligence to indicate that this level of settlement will not be the reality for 2010/11, however it would be an optimistic assumption to think 2011/12 and 2012/13 will see anything more than a cash freeze in resource and the reality may be worse. The cash efficiency targets referred to earlier may be used as the vehicle to justify a nil or even minus level of growth in Formula Grant and DSG.

3.2 It is also quite clear that previous planning assumptions of a 5% increase in Council Tax are no longer tenable, either nationally or locally. In addition the dramatic slow down in housebuilding in the area has had a commensurate effect on the increase in taxbase albeit the allied growth in service will also not have happened.

3.3 The Resource Strategy approved by Cabinet in September 2008 identified a continued growth in high level spending demand particularly for waste services, children's and adults' services. This was predicted at just over £5 million for 2010/11 and £4m for 2011/12, both being pressures in excess of normal pay and price inflation.

Note: as a very simplistic guide a 1% increase in pay is worth a crude £1m cost to the General Fund (non DSG) and non-pay inflation a similarly crude £2 million for each 1% - again non-DSG. The non-pay increase will be netted down by potential increases in income that would reduce the figure to a £1 million per 1%.

3.4 These high level spending needs have been reviewed as part of the preparation of this paper and are narrated and summarised in sections that follow but if the plans already in place are to have credibility then the MTFP for 2010/13 must encapsulate the strategic priorities for Medway as set out in the Council Plan and the targets established for the Local Area Agreement. These present a greater focus than in previous years and are now based on two guiding principles or core values of:

- Putting our customers at the centre of everything we do; and
- Giving value for money.

These themes are exemplified under the six key outcomes as follows:

- A clean and green environment
- Safer communities
- Children and young people having the best start in life
- Older and vulnerable people maintaining their independence
- People travelling easily and safely in Medway
- Everyone benefitting from the area's regeneration.

4. Assessment of Likely Available Resources

4.1 The size of the Council's revenue budget is determined by two major factors:

- The support from central government by way of Formula Grant and Dedicated Schools Grant (DSG); and
- The amount raised locally by council tax.

4.2 With regard to central government funding, the Local Government Finance Settlement for 2010/11 will be the last year of a three year settlement announced on the back of the outcome of the last Comprehensive Spending Review (CSR2007). Accordingly Government support for 2010/11 is known with relative certainty. The next Comprehensive Spending Review will be CSR2010 and unsurprisingly this is scheduled to be announced in the summer/autumn of 2010 a few months after the General Election. There is some suggestion that for 2011/12 there may be a one year settlement with the CSR planned being deferred a year to permit the incoming Government to take stock. At this stage it is, therefore, only possible to make an estimate of the potential settlement and that is against a background of tremendous uncertainty for public sector spending as a whole. For planning purposes it is suggested that a nil increase is assumed recognising that this may be an optimistic view.

4.3 For council tax increases, the present Government has shown no sign of softening its approach to ‘capping’. For 2009/10 this was again enforced and whilst no expectation has been declared it is unlikely, given the recession and the current rate of inflation, that a 5% ‘cap’ will be maintained. It will therefore be prudent to assume that the 5% target imposed for this year, to keep council tax in ‘low single figures’, is likely to be reduced. This will not assist our relative position, given the low baseline that we continue to have (6th lowest Unitary and 24th lowest nationally).

4.4 The taxbase upon which the current Council Tax is set was agreed as 86,098 Band D equivalents. As at the end of August that had risen to 86,567 - an increase of 0.5% and 469 properties. New building does continue in the borough albeit at a reduced rate to expectation a year or so ago. Care also has to be taken in that there is a significant exemption/discount factor with, for example, some one third of dwellings claiming single person occupancy discount at 25%. Nonetheless it is reasonable to expect some growth in the yield arising from an increase in the taxbase and this is expected to be 0.75%, 0.5% and 0.5% year on year for 2010/13.

4.5 For DSG there is some logic in an expectation of a slightly better position than that for Formula Grant and it is suggested that a +1% per pupil scenario for 2011/13 is used together with indicative 2010/11.

4.6 Table 1 below illustrates potential resources for 2009/13 based upon the assumptions in 4.2 to 4.5.

Table 1: Potential Resources for 2009/2013

Description	**2009/10**	**2010/11**	**2011/12**	**2012/13**
	£m	**£m**	**£m**	**£m**
Formula Grant - % Increase	**4.0%**	**+3.6%**	**+0%**	**+0%**
- amount	**82.225**	**85.130**	**85.130**	**85.130**
		+0.75%	+0.5%	+0.5%
Taxbase	86,098	86,744	87,178	87,614
Council Tax (£1,092.33 baseline)	**94.048**			
Increase @ +3.0%		**97.600**	**101.030**	**104.580**
DSG (based on forecast pupil numbers)	**167.458**	**172.140**	**171.830**	**171.360**
Pupil Numbers	**40,074**	**39,560**	**39,098**	**38,605**
Funding per pupil £	**4,179**	**4,351**	**4,395**	**4,439**
Summary Resources:				
DSG	**167.458**	**172.140**	**171.830**	**171.360**
% Increase (per pupil)	**+3.59%**	**+4.13%**	**+1.0%**	**+1.0%**
Non-DSG (Council Tax @ +3%)	**176.273**	**182.730**	**186.160**	**189.710**
% Increase	**+4.63%**	**+3.66%**	**+1.88%**	**+1.91%**

4.7 The sensitivities around Table 1 are important and for Formula Grant a 1% reduction from that predicted would be £851,000 and for Council Tax a 1% change is almost £l million. For DSG the position is complicated by the forecast pupil numbers but if the per pupil increase were to move by 1% that would represent £1.7 million of grant change

4.8 In addition to the revenue resources evidenced by the table above the council does have access to reserve balances, however, the balance of General Reserves (i.e. those not allocated for an earmarked purpose), whilst increased as a result of last year's favourable outturn, is still at a minimum level. Any possible underspending from 2009/10 could be available although prudence would dictate that reserves are built up from present levels.

4.9 For 2010/11 an average increase in non-DSG resource at almost 3.7% (assuming council tax increases at 3%) is likely to be in excess of pay and general price inflation and will therefore contribute towards other expenditure pressures. For future years the increase is unlikely to cover inflationary pressures. Increases in the DSG are marginally better in 2010/11 but worse for future years and coupled with a forecast fall in pupil numbers will produce a cash reduction in the overall level of funding.

4.10 With falling pupil numbers driving a reduced level of DSG, and pay costs for non-teaching staff likely to present a greater demand because of the incremental scales and pension costs, there is a likelihood that the centrally retained component of the DSG will yet again be subject to greater pressure in the face of escalating demand.

5. Spending Priorities

5.1 It is not the purpose of this document to plan the service needs of departments but nonetheless there are a number of key spending issues that sit alongside the priorities of the council. These are highlighted below and set out in the table that follows.

Regeneration and Development

- A number of areas where the non-recurrent effects of the recession upon service delivery are expected to be felt into 2010/11 to the extent of £0.3m;
- The impact of the Olympics in 2012 both directly in terms of income loss and indirectly in promoting the tourism offer will impact upon revenue to the extent of £0.3m;
- Ongoing over optimism in relation to income receipts from the Leisure portfolio presents a recurrent pressure of £0.3m in addition to the recessionary difficulties above;
- The FUSE festival has established itself as a significant cultural event in the South East but to maintain Arts Council grant and add Youth FUSE to the programme is a further £0.1m demand;
- The agreement to be concluded on the Medway Tunnel will pass ownership and responsibility for maintenance in whole to the Council. There is a limited reserve available to offset these costs, which are currently running at some £1m a year and, at this rate, the sum will be exhausted before the period under review. Efforts are continuing to seek

Government support for the tunnel in common with all other strategic routes such as that upon which the tunnel sits;

- The new Urban Traffic Management control system will require revenue support for maintenance and running costs of the control room and systems with a recurring demand for £0.1m;
- The capital works to improve bus operations and the quality transport corridor have a recurrent revenue legacy for operating and maintenance costs of £0.25m; and
- Preparation of the new LTP will require non recurrent consultant support of £0.1m.

Children's and Adult Services

Children and Adult Services is the largest directorate, representing the largest call on available resources, and it is subject to an increasingly rigorous and challenging inspection regime, which will have a significant impact on the Council's overall CAA rating;

- The current spending forecasts for the directorate reveal ongoing demographic pressures on key, demand-led, services for the elderly and disabled. It is anticipated that demographic growth in elderly care, physical disability care and learning disability care will cost £0.6m, £0.2m and £0.3m respectively for 2010/11 and further similar pressures beyond. Against this there are potential savings from the enablement agenda and extra care of some £0.8m for future years;
- Mental health services and the operation of the Section 75 lead commissioning arrangements are being reviewed but it is expected that pressures of up to £0.2m will be highlighted in this area;
- For children's social care there are pressures on services outside of the DSG, most notably to implement changes arising from the recommendations of the Lord Laming review £0.7m; the 'Mumby' ruling in the courts that demands equality in payments to relatives or foster parents, £0.2m and the recent Law Lords ruling that homeless 16-18 year olds should be entitled to leaving care support will add a further £0.6m to the costs of 'Looked After Children';
- The requirements of the 'Public Law Outline' were discussed and estimates included in current budgets. It is not yet clear as to the accuracy of these estimates but if the limited number of assessments undertaken so far are a reasonable reflection of ongoing requirements there could be a further pressure on budgets of some £0.7m;
- For non DSG/non social care issues for young people there are pressures for additional staffing to support Youth Rehabilitation Orders that commence in September 2009 of £0.1m and the current service offered by the 'Onside Project' to help avoid expensive permanent exclusions is funded by a grant from the De Haan Trust that ceases this year and will create a pressure for 2010 and beyond of £0.1m;
- The major part of the directorate service provision is funded by the DSG and to that extent service growth will be determined by the additional funding provided by Government through this means. However there is a balance within the DSG between the funds delegated to schools and the funds retained centrally to manage other pupil services. The level of retained funding is restricted by the 'Central Expenditure Limit' (CEL). In recent years there has been sustained growth pressure within SEN services particularly in relation to independent and non-maintained sector

placements and these are forecast to grow further at £0.7m, These form part of the CEL and whilst the 'headroom' between the minimum funding guarantee to schools and the actual DSG may be used to support growth it has to be with the agreement of the Schools Forum. It is going to be very difficult to get such an agreement if schools budgets are going to be under the pressure anticipated for 2011 and beyond; and

- The closure and mergers programme necessary to effectively plan for pupil demographics is also likely to generate costs that under current arrangements fall to the non-schools component of the DSG. These will include redundancy, retirement and deficit balances where they exist. Estimating such costs in advance is clearly very difficult but initial forecasts suggest a non-recurring pressure upon the DSG of £1.3m and the General Fund (redundancy/retirement) of £0.2m.

Business Support/Corporate Issues

- There is a need to fund the non-recurring support that was provided to the 2009/10 budget This was £1m from the 2008/09 underspend, £0.5m from miscellaneous reserves, £0.25m from the Local Authority Business Growth Incentive (LABGI) scheme, £0.5m from VAT recovery and £1.1m from the Supporting People reserve – a total of £3.35m;
- The pay provision in the 2009/10 budget was set at 2% and with the latest employer offer at 1% there is a potential saving of £0.8m;
- Employer pension contributions are likely to increase following the 3 yearly valuation of the LGPS fund due at 31 March 2010, given the fall in the value of equities that form a substantial part of the fund balance (£0.771bn of the total £1.974bn investment at 31 March 2009 but a drop of £0.337bn in market value from the previous year). This is difficult to predict at this stage and there are national measures being suggested to mitigate the effects. However for prudence it is assumed that a 2% increase in employer contribution will be required, spread over the 3 years to the next valuation. This would represent a £0.5m pressure compounding for each of the next 3 years; *(current contribution rate is circa 21%)*;
- New borrowing to support capital investment outside of the 'prudential' regime is funded by incorporation in the grant formula and is therefore incorporated in the resource tables above. However it is not in the current budget and such 'supported borrowing' is running at about £10m pa with an associated cost for interest and principal of £1m pa in incremental addition through the period; and
- Pay and Prices for both the General Fund and the DSG are crudely estimated at £3 million each, representing an overall level of 2%.

Table 2: Summary Additional Resource Requirement – against 2009/2010 base

	2010/2011	2011/2012	2012/2013
	£m	£m	£m
Pay/Price Inflation @2%			
General Fund	3.000	3.000	3.000
DSG	3.000	3.000	3.000
Regeneration, Community and Culture			
STG income shortfall	0.120	(0.120)	
Leisure income shortfall	0.450	(0.150)	
Theatre income shortfall	0.050	(0.050)	
Income loss (Olympics)		0.100	0.100
Tourism marketing (Olympics)		0.100	
FUSE	0.050		
Medway Tunnel		1.000	
Traffic control system		0.040	0.035
Chatham Bus Station		0.150	
Quality Transport Corridor		0.100	
LTP preparation	0.100	(0.100)	
Adults and Children			
Elderly/Disability Care	1.106	1.130	1.747
Enablement Project		(0.540)	
Extracare			(0.210)
Mental Health statutory services	0.200		
Laming	0.670		
Mumby ruling	0.230		
Looked After Children	0.654		
Public Law Outline	0.658		
Youth Rehab Orders	0.100		
Onside Project	0.100		
SEN (DSG)	0.730	0.750	0.820
School Mergers & Closures (DSG)	1.300	(1.300)	
School Mergers & Closures (Non DSG)	0.200	(0.200)	
Business Support/Corporate Issues			
Non Recurring Support removal	3.350		
Pay saving ex 2009/10	(0.800)		
Pensions		0.500	0.600
Debt Financing	1.000	1.000	1.000
TOTAL -GENERAL FUND	**11.238**	**5.960**	**6.272**
-DSG	**5.030**	**2.450**	**3.820**

5.2 This is not an exhaustive list and is focussed on the pressures that already exist or are seen as unavoidable. Inevitably there will be many enhancements to service that the Council would also wish to see, but as a summary of the larger issues already presenting as probable pressures, they tabulate to a sizeable challenge for re-directing resource. Table 3 below summarises the net effect of these amounts when compared to additional resources as set out in Table 1.

Table 3: Net Resources

	2009/10	2010/11	2011/12	2012/13
	£m	£m	£m	£m
DSG	167.458			
Additional DSG (based on forecast pupil numbers)		4.682	(0.310)	(0.470)
Additional Resource Demand		5.030	2.450	3.820
Net Surplus/(Deficit)		(0.348)	(2.760)	(4.290)
Summary Resources:				
General Fund	176.273			
Additional Grant/Ctax		6.453	3.430	3.551
Additional Resource Demand		11.238	5.960	6.272
Net Surplus/(Deficit)		(4.785)	(2.530)	(2.721)

6. Balancing Resources and Demands

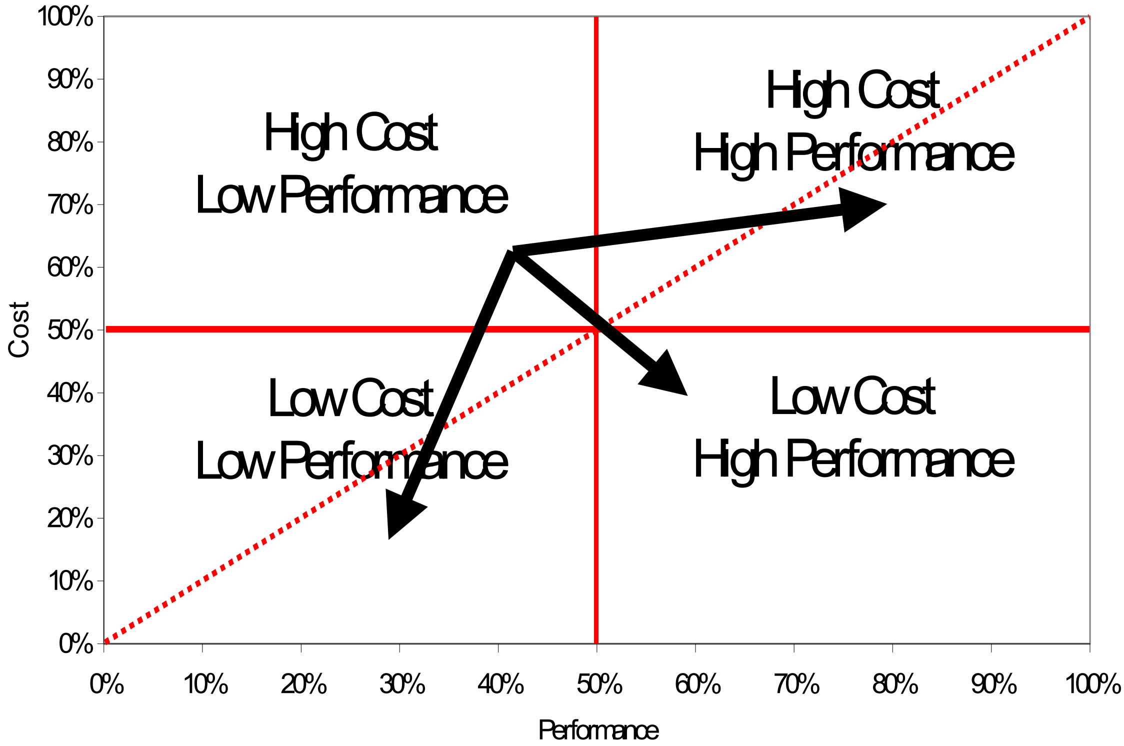
6.1 There is a need to make immediate progress in a number of areas where there are potential efficiencies to be gained without impacting significantly on service delivery to residents. Initial areas to be covered are:

- Linked Service Centres review;
- SEN re-provision;
- Enablement (including extra care);
- E-back office;
- Property rationalisation;
- Opportunities for market testing; and
- Review of pay and allowance issues.

6.2 In addition to the areas identified above it is important that the Council embarks upon a rational review of costs, performance and priorities. Whilst our overall score for Use of Resources has been consistently that of a ‘GOOD’ Council, there have been criticisms of our ability to get underneath the more high level picture of cost and performance. The new performance monitoring system ‘Covalent’ provides a tool for collating this information but it has to be collected and analysed in a systematic way. This is consistent with the approach to ensuring Value for Money is embedded throughout the organisation and is not a high level view.

6.3 Medway has adopted Value for Money (VFM) as one of it’s two core values. However as a Council we have no VFM strategy, nor do we have a robust and consistent mechanism for demonstrating that this is achieved and maintained. Officers have looked at examples of best practice in exemplar authorities and the lessons learned will be applied to Medway. As a beginning a VFM Strategy has been drafted and is attached as Appendix 1. This is not a document that suggests dramatic change but rather re-enforces good practice and is a reference point for understanding what that core value should represent. It will be supported by a performance monitoring and service planning regime that identifies both costs and performance of services and a mechanism to demonstrate VFM through service self assessment.

6.4 This will be important for the future direction of resource equalisation. As the diagram below shows the exposure of cost and performance relative to priority enables a better informed approach to organisational change.



6.5 The analysis is fairly obvious with high cost/low performance being a primary target for change. In priority services it may be an issue of high cost being acceptable but the focus should then be on matching performance to cost. In non priority services, aside from the question as to whether they continue, there ought to be an emphasis to at least drive costs down, preferably with an improvement to performance.

6.6 Such an approach may involve:

- radical service re-design;
- new ways of working;
- systematic, continuous improvement; or
- a combination of all.

7. Timetable

7.1 The timetable for production of the Medium Term Financial Plan and Draft Budget Proposals is as follows:

Report to Cabinet	22 September 2009
Report to Overview & Scrutiny	15 October 2009
Portfolio/Directorate reviews	September to November
Initial budget proposals to Cabinet	24 November 2009
Reports to Overview & Scrutiny	December/January
Draft budget to Cabinet	16 February 2010
Budget proposals to Council	25 February 2010

7.2 Business and service planning will run in tandem with the budget setting process.

8. Conclusion

8.1 The Medium Term Financial Plan identifies our spending needs for 2010/11 and beyond. It is clear that there is a need to both curtail aspirations and identify efficiencies and changes to service delivery to produce a balanced financial position over the next three years even with a fairly optimistic view of resources. The efficiency agenda must assist with this and Government assumptions around the 4% per annum cash target and potentially enhanced levels for 2011/13, discussed in section 2.4, would clearly deliver this if those efficiencies were realised.

8.2 Irrespective of the forecast shortfall in resources arising from the budget requirement, it must remain the Council's main strategic aim to achieve a sustainable budget without recourse to reserves. To that effect it is critical that both existing and emerging requests for pressures are challenged out of the process where possible and that due weight is given to driving forward the efficiency agenda and the search for more radical and cost effective means of delivery. The VFM strategy and more specifically the measures described in section 6 will be a key part of that process over the term of this plan.

8.3 This report was considered by Cabinet on 22 September and Members:

- Endorsed the underlying aims of the Medium Term Financial Plan;
- Endorsed the forecast level of overall funding outlined in Section 4.6;
- Instructed portfolio holders and directors to identify savings and efficiencies to achieve a balanced budget for 2010/2011 and
- Adopted the Value for Money strategy set out at Appendix 1.

9. Financial and Legal Implications

9.1 These are contained within the body of the report.

10. Risk Management

10.1 The risks exposed by a failure to effectively manage the resource planning and allocation process to achieve priorities and maintain effective service delivery are great. The inevitability of elections at both national and local level during the period, the uncertainties about recovery from the current recession and the consequences in terms of future financial assistance and targets imposed by Government will make this process difficult.

10.2 In monetary terms the impact of the recession is having a significant effect upon Council resources with fees and charges representing a greater income stream than Council Tax and there is a clear risk that it will take longer than expected to see a return to pre-recession levels. Formula Grant and DSG are but one aspect of Government funding with a significantly greater sum being received through specific grants and Area Based Grant. All of these funding streams are at risk in the absence of clarity about the next spending review period.

11. Recommendations

11.1 Members are requested to consider the Resource Strategy 2009/2012 and make comments to the Cabinet.

Background Papers

Resource Strategy – Report to Cabinet 23 September 2008.
Capital and Revenue Budgets 2009/2010 – Report to Council 26 February 2009.
Medium Term Financial Plan 2010/2013 – Report to cabinet 22 September 2009.

These reports are available via the Council's website: www.medway.gov.uk

Medway
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