HAMBLETON DISTRICT COUNCIL

Report To: Cabinet
6 February 2018

Subject: **FINANCIAL STRATEGY 2018/19 TO 2027/28**

All Wards

Portfolio Holder for Economic Development and Finance: Councillor P R Wilkinson

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1.0 PURPOSE AND BACKGROUND:

1.1 The purpose of this report is to consider the Financial Strategy 2018/19 to 2027/28.

Financial Strategy 2018/19 to 2027/28

1.2 The Financial Strategy 2018/19 to 2027/28 is set out in Annex A and Annex A(1) and provides an analysis of the estimated financial position and the direction of the Council's Financial resilience over the next 10 years. It takes into consideration Government funding, other resources, service pressures and priorities and is divided into the following sections:-

- Benefits of and principles underpinning the Financial Strategy for 2018/19 to 2027/28;
- The national economic context;
- Government policy;
- Local Government four year funding settlement 2016/17 to 2019/20;
- New homes bonus;
- Business rates;
- Income generating revenue streams;
- Council tax;
- Local income position;
- Spending pressures;
- Financial risk analysis.

1.3 The key issues for the Financial Strategy are:-

- The impact of the continued reduction in the funding settlement for Local Government from Central Government.

- The calculation of the New Homes Bonus grant and the longevity of this scheme.

- The implication of the new 100% Business Rates Retention Scheme and how this will operate to potentially compensate for the loss of the Government funding settlement.

- Significant income streams to be generated from the commercial strategy, capital schemes and economic development projects across the council.

- The impact of the low Bank Base Rate on the ability of the Council to generate investment income from balances.

- Ongoing spending pressures and the need to realise efficiency savings, whilst continuing to provide a good level of services.

1.4 The Council's financial standing significantly deteriorated as a direct result of the four year funding settlement for 2016/17 to 2019/20 where revenue support grant and rural services delivery grant are to reduce to zero in 2019/20. New homes bonus grant has been assumed to continue through the 10 year financial strategy but this will be closely monitored.

1.5 The introduction of the 100% Business Rate Retention scheme after 2019/20 remains undefined with the Secretary of States announcement in December 2017 that 75% of business rates would be retained in 2020/21 with the local position being fiscally neutral. The level of funding available to support Council's services in future and 100% Business Rate Retention remains uncertain. At this stage, the financial strategy assumes that the Council's funding position and services to be provided (although may alter with increased or decreased service burdens matched with increased or decreased funding) overall will remain constant.

1.6 It should be noted that in November 2017, Cabinet confirmed that the Council would partake in the application to the then Department for Communities and Local Government (DCLG) for a North Yorkshire and East Riding 100% Business Rates Retention Pilot in 2018/19. This pilot scheme was not approved by the DCLG in December 2017 and therefore the Council continue with its Business Rates Pooing arrangements as is consistent with the last there years.

1.7 To maintain a robust Financial Strategy it is vital that the Council generates income using the commercial strategy, from capital schemes and economic development projects across the Council. £7,900,000 is required over 10 years to support the Financial Strategy, starting with £400,000 in 2020/21.

1.8 In achieving these income generating revenue schemes it is anticipated that balances will remain stable throughout the Financial Strategy at between £9,468,436 and £12,175,224, with the 10 year position showing a balance of £10,370,356

2.0 LINK TO COUNCIL PRIORITIES:

2.1 The Financial strategy supports all the Council's priorities to ensure that all services can be delivered in a way that is affordable and sustainable.

3.0 RISK ASSESSMENT:

3.1 There are no risks associated in approving the recommendation.

4.0 FINANCIAL IMPLICATIONS:

4.1 The financial implications are detailed in the body of the report.

5.0 LEGAL IMPLICATIONS:

5.1 There are no legal implications associated with this report.

6.0 EQUALITY/DIVERSITY ISSUES

6.1 There are no equality and diversity implications associated with this report.

7.0 RECOMMENDATIONS:

7.1 It is recommended that Cabinet approves and recommends to Council the Financial Strategy 2017/18 to 2026/27 at Annex ‘A’ and ‘A’(1).

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Background papers: None

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ANNEX 'A'

FINANCIAL STRATEGY 2018/19 TO 2027/28

1.0 PURPOSE OF THE FINANCIAL STRATEGY 2017/18 TO 2026/27:

1.1 The Financial Strategy is a key aspect of the Council's Budget Policy Framework. It aims to ensure that resources are aligned to the Council's corporate aims as set out in the Council Plan, as well as delivering customer focused outcomes and continual service delivery improvement. The Financial Strategy sets out the strategic financial position and the financial direction of the Council over the next 10 years taking into consideration the Council's strategic objectives, significant Government grant cuts, other resources and service pressures. The Strategy is regularly monitored and updated to reflect the relentless changes in public sector finance. The key objective of the Financial Strategy is to facilitate the strategic objectives of the Council whilst providing the assurance that the financial standing of the Council over the next 10 years maintains resilience.

2.0 BENEFITS AND PRINCIPLES UNDERPINNING THE FINANCIAL STRATEGY 2018/19 TO 2027/28:

2.1 The benefits of preparing and maintaining the Financial Strategy include that:-

- it provides financial parameters to assist with strategic planning to support the delivery of the Council's strategic objectives;
- it allows the Council to respond to internal and external financial pressures assisting with the development of a sustainable budget over the period of the Financial Strategy;
- it highlights financial risks and mitigating controls promoting the maximisation of resources and the delivery of value for money; and
- it reviews the Council's reserves policy to assist in planning against unforeseen events.

2.2 The principles underlying the Financial Strategy 2018/19 to 2027/28 are set out below:-

- the overall Financial Strategy will ensure the Council's resources are targeted towards meeting its strategic priorities;
- the Council Plan and associated activities will inform a review of the Financial Strategy on an annual basis. The annual review will include an update of the 10 year financial forecast, expected developments within the Council together with the anticipated financial impact of any legislative changes;
- the Council undertakes to maintain its level of expenditure within the boundaries set in the Annual Revenue Budget. If, following monthly budget monitoring, expenditure is expected to exceed original estimates, plans will be prepared detailing the actions required to ensure that spending at the year-end does not exceed the original estimate;
- the Council will maintain its General Reserve at an adequate level to cover any major unforeseen expenditure. The Council will aim to balance its revenue budget without reliance on the use of the General Reserve;

- the Council will maintain earmarked reserves for specific priorities that are consistent with its strategic objectives. The use of these reserves will be consistent with the principles set out in the Financial Strategy and will be reviewed annually;

- the Council will balance the need to increase Council Tax with the delivery of its priorities, taking into account the economic challenges facing its communities;

- opportunities to generate revenue and capital income streams will be sought, along with securing external funding. The implications of the cessation or withdrawal of funding will also be reviewed to ensure that options are considered prior to undertaking income generating and external funding schemes.

3.0 NATIONAL ECONOMIC CONTEXT:

Brexit

3.1 The UK economy weathered the initial shock of the Brexit vote during 2016/17, however in 2017/18 sterling has devalued and growth fallen. For 2018/19 and going forwards the Chancellor revised the growth forecast down to 1.5% in the autumn budget. On 8 December 2017, the UK and European Commission reached an agreement to move talks on BREXIT forward and specifically in relation to this EU/UK agreement there are five areas that are most important to Local Government – Workforce, Devolution in the UK, EU Funding, The European Investment Bank and Customs and trading Standards. The council continues to consider the impact of BREXIT on the financial strategy and will update Members when appropriate.

Inflation

3.2 In 2016, after the UK surprised on the upside with strong economic growth, growth in 2017 has been disappointingly weak; the main reason for this has been the sharp increase in inflation, caused by the devaluation of sterling after the EU referendum, feeding increases in the cost of imports into the economy. The Consumer Price Index (CPI) inflation peaked at 3% in 2017, with the forecast for Consumer Price Index (CPI) inflation to fall back to near its target rate of 2% in two years' time. Low Wage inflation is a common factor in nearly all western economies as a result of automation and globalisation however the Bank is also concerned that the withdrawal of the UK from the EU would effectively lead to a decrease in such globalisation pressures in the UK, and so this would cause additional inflationary pressure over the next few years. The positon will continue to be monitored in relation to bank base rate.

Bank Base Rate

3.3 The Monetary Policy Committee (MPC) as expected delivered a 0.25% increase in Bank Rate at its meeting on 2 November 2017 due to increase in inflation. This removed the emergency cut in August 2016 after the EU referendum. The MPC also gave forward guidance that they expected to increase Bank rate only twice more by 0.25% by 2020 to end at 1.00%. These continued low rates of interest have a significant impact on the Council's ability to generate investment income and will continue to be regularly monitored and revised

4.0 GOVERNMENT POLICY AND IMPACT:

4.1 Government policy for the provision of funding for local authorities has significantly changed since 2010 with the focus being on reduced Government grant funding, the drive for increased efficiencies and the development of alternative funding methods.

Spending Review 2010

4.2 The main emphasis of Spending Review 2010 was to significantly reduce public sector spending to facilitate a reduction in the UK's borrowing deficit. Based upon Spending Review 2010 the Local Government finance settlement for 2011/2012 and 2012/2013 was announced on 11 January 2011. This resulted in a reduced finance settlement for the Council of over £1.6m or 29% across the period.

Spending Round 2013

4.3 Spending Round 2013 was announced in June 2013, this set out in broad terms the funding envelope for Local Government for 2014/15 and 2015/16. It was estimated that the Council would lose an additional 21% of its funding from Central Government over the 2 year period. However, further cuts increased this to almost 25%.

Four Year Settlement March 2016

4.4 The announcement in the December 2015 autumn statement confirmed the Government would provide four year funding settlements for local authorities. This increases the certainty for Council's to plan for the medium term when there is continued deterioration in grant funding. The Financial Strategy estimated that this Council will lose 22.4% of its grant funding from Central Government excluding New Homes Bonus Grant over the 4 year period 2016/17 to 2019/20. In order to sign up for the four year funding settlement an Efficiency Plan had to bed to be published by October 2016, this Council's Efficiency Plan was approved at Council in September 2016.

Autumn statement 2017

4.6 The four year funding settlement for the 2018/19 financial year was confirmed by the Department for Communities & Local Government (Since renamed to Ministry of Housing, Communities & Local Government) on 19 December 2017. The headline Core Spending Power nationally is expected to increase by 1.5%, where the national reduction in revenue support grant -6.4% is offset by the expected increase in council tax, 7.8%. The Core Spending Power is the overall impact on local authorities of changes in funding and locally-raised council tax

4.7 The Core Spending Power for this Council in 2018/19 has decreased by -0.38% which was mainly due to the significant fall in revenue support grant which is offset by the increase in Council tax and the increase in the number of properties in the district.

5.0 LOCAL GOVERNMENT FINANCE SETTLEMENT AND THE IMPACT OF THE NEW 100% BUSINESS RATE RETENTION SCHEME:

5.1 The indicative four year funding settlement released by the Government in December 2015 provides details of the baseline funding allocations which supports local authorities – for this Council this is mainly revenue support grant, rural services delivery grant, new homes bonus, business rates and council tax which are collected locally. The provisional financial settlement indicates that by 2020 revenue support grant and rural services delivery grant will cease, resulting a further reduction of funding to the council of £1.6m.

5.2 The business rates that are collected locally are one of the funding sources (along with government grants and council tax) that support the Council's net budget. The business rate retention scheme was part of the new funding mechanism introduced for Local Government on 1 April 2013 and it enables Councils to keep a proportion of the business rates collected locally, providing an incentive for Councils to grow their local economy.

5.3 The proportion of income retain under the Business Rate Retention funding model was in relation to business rates growth above the Government target where 40% was retained by the District Council, 18% by the County Council, 2% by the Fire Authority and 50% was returned to Government.

5.4 The scheme has developed since 2013 with the Government allowing the Council to enter a Business Rate Pool with other local councils in North Yorkshire (excluding Selby District Council and Harrogate Borough Council). The effect of this pool is that any business rates collected by pool members above the Government’s target will be retained by the pool, 50% will not be forfeited to Central Government as described in the paragraph above. The Business Rate Pool continues to operate in 2018/19.

5.5 In future, with the loss of grant funding from Government, the business rate retention scheme is to be further developed by Government with the proposal that local authorities will retain 100% of business rates. Government consulted on 100% business rate retention in September 2016 but this process has currently stalled with no new primary legislation being introduced in the Queen’s speech in May 2017 due to the Governments involvement in BREXIT. In the autumn statement an extension to the current business rate retention scheme was announce for 2020/21 where local authorities will retain 75%.

5.6 The Government continues to support the 100% business rate retention scheme where local authorities assume that with an increase in funding there will also be the responsibility of increased burdens, where Council’s will provide additional services locally. In the main, local authorities also assume that they will be no worse off overall than the current financial position. 100% business arte retention should be fiscally neutral.

5.7 Alongside the 100% business rates retention scheme, to review the overall current financial position of all local authorities the Fair Funding Review consolation is out until March 2018. The fair funding review will set new baseline funding allocations for local authorities by delivering an up-to-date assessment of their relative needs and resources, using the best available evidence. A wide range of options for developing an updated funding formula are being considered by looking again at the factors that drive costs for local authorities and the consultation focuses on the approaches that have been identified to measure the relative needs of local authorities. In the development and changes of the 100% business rate retention scheme there will always be individual winners and losers and further details will be clarified in the next couple of years.

5.8 The Financial Strategy attached at Annex A1 comprises the information provided by the provisional four year funding settlement, an estimate for 2020/21 75% business rate retention and also makes prudent assumptions with regards to the 100% Business Rates Retention scheme. From 2020/21 it is currently assumed that the Council’s position will be fiscal neutral with increased responsibilities and burdens being somewhat matched with 100% business rates retention funding; growth to business rates has been estimated to increase by 2.8%.

6.0 NEW HOMES BONUS GRANT SCHEME:

6.1 The New Homes Bonus grant scheme was introduced in 2011/12 and designed to create an effective fiscal incentive to encourage Councils to facilitate housing growth. The grant is not a ring-fenced grant and is intended to be part of the Council's core funding, as such the Department of Communities and Local Government (now since January 2018 Ministry for Housing, Communities & Local Government) intended the New Homes Bonus grant to be a ‘permanent feature of the Local Government finance system’.

6.2 The Government then published a consultation paper in December 2015 "New Homes Bonus: Sharpening the Incentive" in order to make changes to the scheme from a system with few controls to one that is cash-limited each year. Key changes introduced from 2017/18 and which have remained for 2018/19 are:

- A move to 5-year payments, from 6 years, for both existing and future new homes bonus allocation in 2017/18 and then to 4 years from 2018/19.
- Introduction of a national baseline of 0.4% of housing growth from 2017/18, below which allocations will not be made.
- Government will also retain the option of making adjustments to the baseline in future years to reflect significant and unexpected housing growth. No changes were made in 2018/19 and the baseline remain at 0.4%
- Allocations will continue to be un-ringfenced grant

6.3 The changes were more punitive than expected. For example in the original consultation on New Homes Bonus, the national baseline that was expected was 0.25% for housing growth, below which no funding would be given. It is anticipated that in future te baseline will rise to encourage local authorities to generate housing growth.

6.4 Similar to the Business Rate Retention scheme there is a split of this income, with 80% retained by the District Council, 18% to the County Council and 2% to the Fire Authority. New Homes Bonus represents an opportunity for the Council to generate significant levels of grant that can assist in dealing with the unprecedented levels of formula grant reductions facing the Council.

6.5 Allocations regarding New Homes Bonus in the Financial Strategy for 2018/19 and 2019/20 are as detailed in the four year funding settlement at £1,541,827 and £1,635,370 respectively. There after the assumption that around £1,000,000 will be received is included each year and reflected in the Financial Strategy at Annex A1.

7.0 INCOME GENERATING REVENUE STREAMS:

7.1 In 2018/19, due to the reduction of Government grants, the council needs to look for other sources of funding to support the future revenue budget and the ongoing financial sustainability of the 10 year financial strategy. Therefore to continue to support services the financial strategy details from 2020/21 that external income will be generated. This does not affect the 2018/19 budget or the position on Council Tax 2018/19 but it should be noted that plans are in place to ensure the Council's future level of reserves.

8.0 LOCAL INCOME POSITION:

Council Tax

8.1 The Localism Act 2011 gives a provision for a referendum to veto excessive Council Tax increases. This effectively places a limit on the level of Council Tax set by the Council. If the Council exceeds the Government's prescribed limits the public would be able to vote to agree or veto any considered 'excessive' increase.

8.2 The potential additional cost of a referendum and re-billing would be significant and negate the benefit from the Council Tax increase. Therefore increasing Council Tax above the prescribed limits would require careful consideration.

8.3 The Government has currently prescribed, in December 2017, a limit for the increase in Council Tax at below 3% or £5. The Financial Strategy assumes a prudent increase in Council Tax of £5 on a Band D equivalent property per annum for the duration of the Strategy.

Interest on Balances

8.4 Given the continued low Bank Base Rate, the revenue budget for interest on balances has been set at a prudent level. The Financial Strategy has been prepared on the basis that the Bank Base Rate will remain at 0.5% for 2018/19 with the level of interest rates remaining low and rising to 1% by 2020/21, with only small increases beyond that date. This is consistent with the latest projections on the Bank Base Rate from the Bank of England and other City Institutions.

Fees and Charges

8.5 Fees and charges levied by the Council provide a significant source of income and facilitate reinvestment in Council services. The Financial Strategy assumes all fees and charges increase by 1.56% in 2018/19 and then overall by 2% for the duration of Strategy. In future years the Council will give consideration to the impact on its services, local economic circumstances and the Financial Strategy in applying appropriate fees and charges.

Capital and Prudential Borrowing

8.6 All revenue implications associated with the capital programme are considered when setting the capital programme and revenue budget 2018/19. The Council has taken the decision to fund the Capital Programme via reserves with the exception of potentially borrowing £25m to £36.2m to finance the funding provided to a local Housing Association and the Business Improvement District as part of the development of the Dalton Bridge Scheme. The borrowing will be funded through a mix of using internal borrowing - the Council's own resources - and external prudential borrowing. This mix will ensure the maximum interest receipt return to the Council whilst maintaining a robust cash flow.

Reserves and Balances

8.7 The Local Government Finance Act 1992 requires Local Authorities to have regard to the level of reserves needed for meeting estimated future expenditure when calculating the budget requirement. In establishing reserves the Council must comply with the Code of Practice on Local Authority Accounting in the United Kingdom.

8.8 The provision of an appropriate level of reserves and balances is a fundamental aspect of prudent financial management. Their purpose is to provide for unexpected adverse changes in income and expenditure levels and to provide funding for specific initiatives. This is consistent with the Reserves and Balances Policy adopted by the Council in setting the 2018/19 Council Tax in February 2018.

8.9 The detailed Financial Strategy Annex A(1) shows that the financial resilience of the Council is underpinned by a number of factors:-

1) maximising income generating projects - the interest receipt from the loan to the local Housing Association and charging for green waste;
2) revenue levels will be maintained as far as possible to maximise interest income and maintain borrowing at low levels to support the revenue budget through the tax-payers reserve;
3) generating significant income streams from 2020/21 in accordance with the commercial strategy;
4) the New Homes Bonus Grant will continue to be paid throughout the 10 years;
5) the four year funding settlement is included to 2019/20;
6) the retention of a maintained level of business rates;

7) a prudent increase in Council Tax of £5 on a Band D equivalent property per annum is included for the duration of the Strategy

8.10 It is anticipated in the Financial Strategy for 2018/19 the Council will have Reserves and Balances of £11,509,765. This provides the Council with a strong financial position to deal with the future financial challenges it is facing.

9.0 SPENDING PRESSURES:

Pay

9.1 The National Employers, who negotiate pay on behalf of 350 local authorities, have suggested that the majority of employees should receive a 2% increase for 2018/19 and a further 2% for 2019/20. Those workers on lower salaries would receive higher increases. For fulltime equivalent employees currently on the bottom of the pay scale, the offer would increase their hourly rate from £7.78 now to £9.00 in April 2019. National Employers said it would add another 5.6% to the national pay bill over the two years covered by the offer. This offer has yet to be confirmed but has been built into this Council's Financial Strategy.

Pensions

9.2 The actuarial review of the North Yorkshire Pension Fund has been undertaken at 31 March 2016 which provides the pension cost information for three years to 2019/20. The Pension Fund appointed a new actuary – Aon - for the recent actuarial review whereby assumptions for contributions in the past and for current contributions to be made have changed. The approach taken has reduced the deficiency contribution payments which are necessary to be made for the past but also the current contribution rate has increased. Overall, taking deficiency payments and current contributions into consideration, the budget position for the Council and financial strategy have not changed. With the completion of the actuarial triennial review of the North Yorkshire Pension Fund in December 2016, the Council also made the decision to make a lump-sum contribution with regards to the deficiency payment; this will reduce the annual revenue payments over the next three years by a total of £36,000.

Recycling Contract

9.3 The recycling market is volatile with the Chinese market reducing the amount of plastic recycling it accepts. The council's recycling contractors have been aware of this since the summer 2017 and therefore have been utilising alternative sipping channels other than China to reduce the effect on the council. The quarterly movement of the recycling market is continually being reviewed and the effect taken into account during quarterly monitoring reports. The Financial Strategy has assumed that this position will not worsen in the foreseeable future.

Energy prices

9.4 Energy and vehicle fuel prices continue to be particularly volatile. Prudent provision has therefore been included for continued annual increases in charges for gas, electricity and vehicle fuel for the period of the Financial Strategy.

Capital Programme

9.5 The Financial Strategy provides an estimate of the capital resources that will be required between 2018/19 and 2027/28. The Programme has been constructed to ensure that expenditure is not only maintained within existing resources but that there are capital resources available at the end of the Strategy to provide for the future.

10.0 FINANCIAL RISK ANALYSIS:

10.1 The key financial risks and associated implications for the Financial Strategy are detailed below, a score of high, medium or low has been given to the likelihood of each risk occurring and the impact of risk on the Financial Strategy should it occur:-

Risk	Implication	Prob*	Imp*	Total	Preventative action
Reduction in Government Funding	Loss of income	4	5	20	Lobby Government and respond to any consultations. Budget planning and efficiency savings.
Central Government Policy changes e.g. changes to New Homes Bonus Grant, and 100% Business rate Retention and Fair Funding review for local government	Loss of income	4	5	20	Engagement in consultation and Government policy creation. Communicate to senior management and members the financial impact of changes via the Financial strategy.
Under the Business Rate Retention scheme failure to meet the target for business rate collection set by Government represents a cost to the Council. Also, under this scheme the Government has transferred the risk of business rate no payment to the Council.	Loss of income	3	5	15	Monitor business growth and reduction through collection rates. Act as an enabler with partners on economic development initiatives
New Homes Bonus grant is pivotal to the resilience of the Financial Strategy. Failure to increase the tax base year on year would significantly impinge on this resilience.	Loss of income	3	5	15	Use the Council's powers to encourage house building
Council Tax income levels are not as projected and linked to Government referendum limits	Loss of income	3	5	15	Monitor Government policy and lobby as required. Financial Strategy seminar to Members so they are clearly informed regarding the impact of alternative decisions.
Implications of Devolution and Combines Authority – deal not finalised	Loss of income	3	5	15	Engage in all discussions, be aware of current thinking
Inability to find new income generating revenue streams	Loss of Income	3	5	15	Work started already to find alternative income sources. Future changes built into the Financial Strategy

Risk	Implication	Prob*	Imp*	Total	Preventative action
A continued low Bank Base Rate beyond 2017 would impact on the Council's ability to generate investment income from balances.	Loss of income	4	3	12	Look for other investment opportunities
Fees and charges should be set at a level to maintain a balance between service use and income generation.	Loss of income	4	3	12	Set fees and charges at a fair and reasonable level
Inflationary pressures	Increase in Expenditure	4	3	12	Budget reporting process

Prob = Probability, Imp = Impact, Score range is Low = 1, High = 5