

**FINANCIAL STRATEGY****(Report by the Director of Commerce and Technology)****1 PURPOSE**

- 1.1 The purpose of this report is to assist discussion of the Council's Financial Strategy and obtain the Cabinet's proposals on key aspects. The report will also be considered by the Overview and Scrutiny Panel (Planning and Finance) on 13 September and Cabinet will have the opportunity to consider their comments on 15 September prior to finalising their own recommendations to Council (28 September).

**2 BACKGROUND**

- 2.1 The Council is debt-free and has high levels of revenue and capital reserves which currently provide significant financial flexibility. The Council decided in February that it would use this flexibility to allow modest cash increases in the level of Council Tax each year so that the level of spending reductions required when reserves run out would be minimised. It therefore based the Medium Term Plan on increases in Council Tax of £12 per year. The following table summarises the approved plan:

<b>APPROVED PLAN</b>	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10
	£000	£000	£000	£000	£000	£000
Net Spending before efficiency savings	16,685	17,775	19,670	20,749	22,429	24,116
Efficiency Savings Target	0	-402	-826	-1,273	-1,307	-1,342
<b>Net Spending</b>	<b>16,685</b>	<b>17,373</b>	<b>18,844</b>	<b>19,476</b>	<b>21,122</b>	<b>22,774</b>
<b>Funding</b>						
Total Government Support	-8,731	-9,508	-9,995	-10,481	-10,972	-11,219
Collection Fund Deficit	14	4	0	0	0	0
Council Tax	-5,308	-6,043	-6,790	-7,552	-8,328	-9,120
Use of Reserves	-2,660	-1,826	-2,059	-1,443	-1,822	-2,435
<b>Council Tax</b>	<b>£94.54</b>	<b>£106.54</b>	<b>£118.54</b>	<b>£130.54</b>	<b>£142.54</b>	<b>£154.54</b>
<b>Increase %</b>	<b>14.5%</b>	<b>12.7%</b>	<b>11.3%</b>	<b>10.1%</b>	<b>9.2%</b>	<b>8.4%</b>
<b>Remaining reserves (end of year)</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>
Revenue	17,312	15,486	13,427	11,983	10,162	7,727
Capital	43,038	28,051	17,114	14,864	10,837	5,619

- 2.2 The report to Council also included a graph that showed that service spending would need to be reduced by £4.2M by 2015/16 (in addition to the efficiency savings already included) if Council Tax increases were not to exceed £12 per year in the longer term.

### **3. CAPPING**

- 3.1 Unfortunately, the Government changed its approach to capping this year (it had excluded District Councils taxing at below average levels in 2004/05) and, despite a full explanation of the Council's financial strategy, determined that the Council's budget requirement (Net Spending less use of reserves = £15.547M) would be capped at £15.160M. Cabinet have recommended to Council a revised budget requirement of this sum which results in a reduced Council Tax level of £99.71 for a Band D property. This is a 5.5% increase on 2004/5, and a reduction of £6.83 on what we originally billed.
- 3.2 This reduction results in an extra use of reserves of £387k and an estimated cost of £60k to fund the re-billing exercise.
- 3.3 Inevitably, the possibility of future capping must be taken account of in determining the Council's financial strategy.

### **4. CONTEXT**

- 4.1 Huntingdonshire District Council's Council Tax for the year 2005/06 now compares to that of other Districts as follows (figures in brackets are before capping, where different):
- in the lowest 8% of Council Tax levels for all Shire Districts in England. Range £59 to £275, average £145. The total impact of capping has reduced the District average Council Tax by about 40p.
  - 8.4% (8.9%) of the total Council Tax bill\* for Huntingdonshire residents.

\* *This includes the amounts set by the County Council, the Fire and Police Authorities and Town or Parish Councils.*

### **5. UPDATING LAST YEAR'S BUDGET**

- 5.1 Some of the elements of the Council's finances are broadly outside of its control. Examples include take-up of services, inflation, interest rates, pension contributions and Government Support.
- 5.2 The Financial Strategy takes a longer-term view and, within that time frame, many of its assumptions will turn out to be inaccurate. This is especially true as local government exists in a dynamic environment of political change, both local and national, and increasing customer expectations. Because of these uncertainties the existence of a strategy becomes more important as, each time there is a significant change, the impact on the Council's plan can be identified and addressed.
- 5.3 The first step in the process is to review the assumptions that were included in the approved MTP. A number of adjustments need to be made:

- The impact of the 2005/06 capping.
- Changes in interest rate expectations. The Base Rate was reduced to 4.5% on August 11 and there is general uncertainty about whether another reduction will follow. Fund Managers are therefore only forecasting 4.6 to 4.7% next year and it has been assumed that this rate will continue thereafter. An extra 0.25% would produce an extra £110k next year but as reserves fall in later years the impact becomes insignificant.
- Reassessment of the existing inflation provisions. Electricity supply has just been re-tendered with a 50% increase from October (£140k in a full year) and pay awards are tending to exceed the general level of inflation (3.2% rather than 2.5% this year). It is therefore considered prudent to add an extra 0.5% although this amounts to a significant figure over the forecast period.
- The 2004/05 outturn. Adjustment has been made for deferral of revenue and capital spending to the current year together with additions to reserves to reflect one-off budget savings.
- The 2005/06 capital programme. Deferral of £6.8M from 2005/06 to 2006/07 has already been identified, mostly relating to the replacement of the Council's offices.

5.4 Paragraph 7.1 below further considers the impact of variations from the interest and inflation rates that have been chosen.

5.5 There are also some items that it is not possible to take account of at this stage but will need to be brought into the MTP before it is approved next February. These include:

- Our assumption as to the speed with which the Council will get its additional Government Support (spread over the next 3 years), which may be optimistic.
- Government plans to revise the formulae for distributing Government Support, which are currently the subject of consultation.
- Any revisions to the existing provision for replacing the Council's offices. Additional capital expenditure within the plan period will need to be financed from loan as capital reserves will run out in 2011/12. Each additional £1m of capital expenditure will therefore require eventual reductions in service spending of around £85k per annum to compensate for the extra loan repayments.

5.6 The next step is to consider any general provision for service variations beyond the level to March 2010 agreed in the MTP. It has been assumed that, given the financial position the Council will be facing in the coming years, there should be no additional provision for revenue developments but £3.5M per year for capital investment (at current prices). No allowance has been made for unavoidable additional costs other than the Contingency Reserve (£132k). It has been assumed that any additional items that do not meet the criteria for the reserve would need to be funded from savings.

5.7 The final element is the balance between the use of Reserves and increases in Council Tax. The approach determined in last year's budget was to increase the Council Tax by £12 per year and to reduce spending, in due course, to create a balanced position.

## 6. OPTIONS FOR MEMBER CONSIDERATION

6.1 **Option 1** is based on items described in paragraph 5 above. It is summarised below and additional detail is supplied in Annex A. It represents maintaining the Council's existing strategy.

OPTION 1	2005/6	2006/7	2007/8	2008/9	2009/10	2010/11	2011/12
	£000	£000	£000	£000	£000	£000	£000
Net Spending before savings/reductions	17,569	19,451	20,989	22,777	24,557	26,283	27,627
Efficiency Savings Target	-402	-826	-1,273	-1,307	-1,342	-1,342	-1,342
Additional Spending Reductions	0	0	0	0	0	0	-3,666
<b>Net Spending</b>	<b>17,167</b>	<b>18,625</b>	<b>19,716</b>	<b>21,470</b>	<b>23,215</b>	<b>24,941</b>	<b>22,619</b>
Funding excl. Reserves	15,159	16,394	17,637	18,901	19,937	20,990	22,066
Use of Reserves	2,008	2,231	2,079	2,569	3,278	3,951	553
<b>COUNCIL TAX</b>	<b>£ 99.71</b>	<b>£ 111.71</b>	<b>£ 123.71</b>	<b>£ 135.71</b>	<b>£ 147.71</b>	<b>£ 159.71</b>	<b>£ 171.71</b>
Increase £	£5.17	£12	£12	£12	£12	£12	£12
Increase %	5.5%	12.0%	10.7%	9.7%	8.8%	8.1%	7.5%
Increase % in Budget Requirement	8.1%	8.1%	7.6%	7.2%	5.5%	5.3%	5.1%

### 6.2 Comment on Option 1

For capping, the Government chose authorities which had more than a 5.5% increase in Council Tax AND more than a 6% increase in Budget Requirement. There is no certainty that there will be capping in future years or at what level it would be. Clearly, if the criteria were the same as this year the above option would result in capping next year. Capping would result in a repeat of rebilling costs (circa £60k) and a significant amount of officer time.

Conversely taxpayers understand the £12 a year plan and the public survey showed some support for this level of increase.

The table above goes to 2011/12. Under this strategy, the Additional Spending Reductions required rise to £6.2M by 2016/17. The Council Tax level would be £231.71 in 2016/17.

6.3 Obviously the Council can revise its strategy in any way it chooses but the following two further options seem most relevant in the Council's particular situation.

6.4 **Option 2** is similar to Option 1 except that it is based on retrieving the original plan by recovering from taxpayers over the next 7 years the £6.83 that the Government has required us to reduce Council Tax by this year. Increases would be £13 for the next 6 years, £12.83 for the 7<sup>th</sup> year and then revert to £12. The impact is shown below:

<b>OPTION 2</b>	<b>2005/6</b>	<b>2006/7</b>	<b>2007/8</b>	<b>2008/9</b>	<b>2009/10</b>	<b>2010/11</b>	<b>2011/12</b>
	£000	£000	£000	£000	£000	£000	£000
Net Spending before savings/reductions	17,569	19,450	20,985	22,766	24,537	26,250	27,594
Efficiency Savings Target	-402	-826	-1,273	-1,307	-1,342	-1,342	-1,342
Additional Spending Reductions	0	0	0	0	0	0	-2,322
<b>Net Spending</b>	<b>17,167</b>	<b>18,624</b>	<b>19,712</b>	<b>21,459</b>	<b>23,195</b>	<b>24,908</b>	<b>23,930</b>
Funding excl. Reserves	15,159	16,451	17,753	19,076	20,172	21,288	22,427
Use of Reserves	2,008	2,173	1,959	2,383	3,023	3,620	1,503
<b>COUNCIL TAX</b>	<b>£99.71</b>	<b>£112.71</b>	<b>£125.71</b>	<b>£138.71</b>	<b>£151.71</b>	<b>£164.71</b>	<b>£177.71</b>
Increase £	£5.17	£13.00	£13.00	£13.00	£13.00	£13.00	£13.00
Increase %	5.5%	13.0%	11.5%	10.3%	9.4%	8.6%	7.9%
Increase % in Budget Requirement	8.1%	8.5%	7.9%	7.5%	5.7%	5.5%	5.4%

### 6.5 Comment on Option 2.

The same comments apply as do in Option 1 regarding capping.

It should be possible to explain to taxpayers the logic behind this approach.

Under this strategy, the Additional Spending Reductions required rise to £5.8M by 2016/17.

The Council Tax level would be £238.54 in 2016/17.

6.6 **Option 3** is based on remaining within the Government's 2005/06 capping criteria. Reserves would be used to keep the budget requirement increase down to 6% whilst maintaining our spending plans for as long as possible. While this means that Reserves are used more quickly, this is compensated for by higher Council Tax increases from 2009/10 onwards.

<b>OPTION 3</b>	<b>2005/6</b>	<b>2006/7</b>	<b>2007/8</b>	<b>2008/9</b>	<b>2009/10</b>	<b>2010/11</b>	<b>2011/12</b>
	£000	£000	£000	£000	£000	£000	£000
Net Spending before savings/reductions	17,569	19,454	21,011	22,831	24,652	26,384	27,646
Efficiency Savings Target	-402	-826	-1,273	-1,307	-1,342	-1,342	-1,342
Additional Spending Reductions	0	0	0	0	0	-2,999	-4,800
<b>Net Spending</b>	<b>17,167</b>	<b>18,628</b>	<b>19,738</b>	<b>21,524</b>	<b>23,310</b>	<b>22,043</b>	<b>21,504</b>
Funding excl. Reserves	15,159	16,069	17,033	18,055	19,138	20,287	21,504
Use of Reserves	2,008	2,559	2,705	3,469	4,172	1,756	0
<b>COUNCIL TAX</b>	<b>£99.71</b>	<b>£106.04</b>	<b>£113.26</b>	<b>£121.23</b>	<b>£134.19</b>	<b>£147.91</b>	<b>£ 162.37</b>
Increase £	£5.17	£6.33	£7.22	£7.97	£12.96	£13.72	£14.45
Increase %	5.5%	6.3%	6.8%	7.0%	10.7%	10.2%	9.8%
Increase % in Budget Requirement	8.1%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%

### 6.7 Comment on Option 3

If capping continued and the 2005/06 criteria were retained the Council would not be capped. Unfortunately there has been, and is unlikely to be, any certainty or consistency of approach by the Government. Thus, all that can be said is that there would be less likelihood of capping and

the Council could demonstrate it was reacting in a positive way to the Government's wishes.

It could be explained to taxpayers that the Council is attempting to comply with the Government's wishes.

Under this strategy, the Additional Spending Reductions required rise to £5.2M by 2016/17.

The Council Tax level would be £247.62 in 2016/17.

6.8 Whichever option is chosen, **major efficiencies / spending cuts will be required in service developments already included in the MTP and / or in existing services**. The Customer Consultation Survey and the Council's targets will provide a starting point for this prioritisation but it will be necessary to determine the relative importance of potential options within that framework.

6.9 These reductions are shown in the year when they become inevitable. In practice, the best approach will be to achieve savings and / or make cuts progressively by the required dates.

## 7. SENSITIVITY

7.1 Option 1 has been adjusted for changes in some factors, to see if they have a significant impact. The table below shows the factor that has been changed and the resulting change in the level of savings required.

	First year in which savings are required	Impact	
		Variation in savings required	
		Total to March 2017 £M	Permanent per year by 2016/17 £M
<b>OPTION 1 (as above)</b>	<b>2011/12</b>	-	-
<b>With</b> Interest rate variations			
0.25% increase from 2006/07	2011/12	-0.3	0
0.25% decrease from 2006/07	2011/12	+0.3	0
<b>With</b> Inflation variations			
0.25% increase from 2006/07	2010/11	+4.2	+0.7
0.25% decrease from 2006/07	2011/12	-4.1	-0.7

## 8. REDUCING THE LIKELIHOOD OF CAPPING

8.1 Attempts are being made, via the LGA, to persuade the Government to consider a range of areas where they could provide some comfort short of pre-announcing the capping levels (which they adamantly refuse to do). These areas include:

- No capping for an authority that has a council tax that is below average for its class.
- No capping that would result in a refund of less than £x per year.
- No capping that would result in a refund of less than x times the re-billing cost.

- Capping rules to recognise an additional test e.g. more than X% increase in budget requirement and more than Y% increase in Council Tax **and** more than Z% increase in “service spending” (budget requirement after excluding use of reserves).

**8.2** It is possible that there will not be any certainty as to whether these attempts have been successful in time to influence the 2006/07 budget decisions.

## 9. CONCLUSIONS

9.1 Cabinet, and subsequently Council, are faced with a decision which revolves around the Government’s future attitude to capping District Councils that currently have low levels of Council Tax.

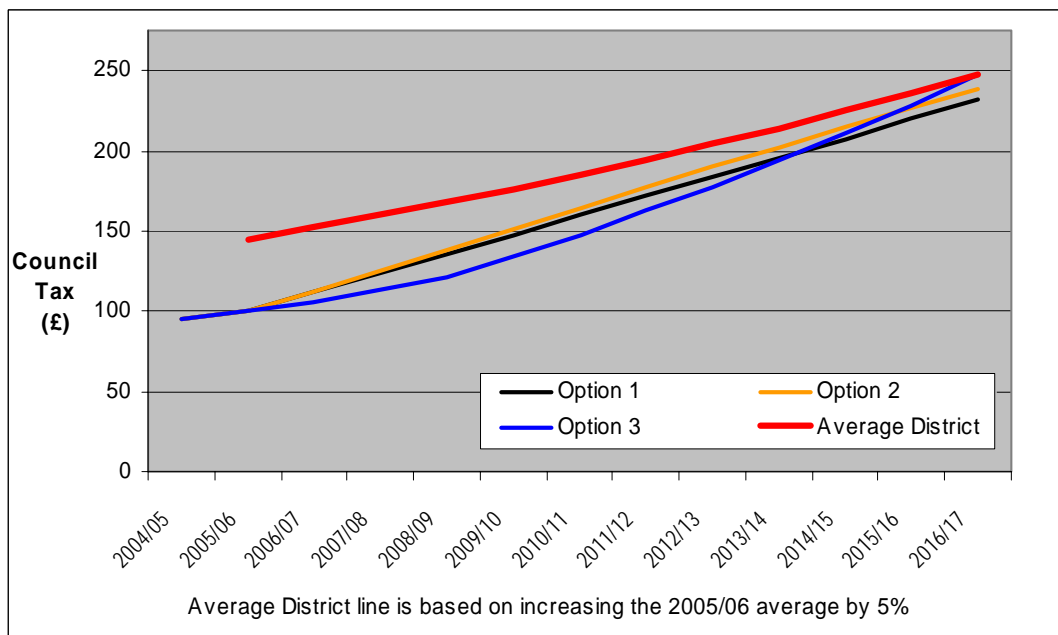
9.2 Fortunately, the Council’s reserves still allow some flexibility if the Council were to agree a strategy that resulted in the Council being capped again.

9.3 None of the options illustrated in this report guarantee that the Council will not be capped either in 2006/07 or later years. Each requires eventual reductions in service spending of over £5.2M per year.

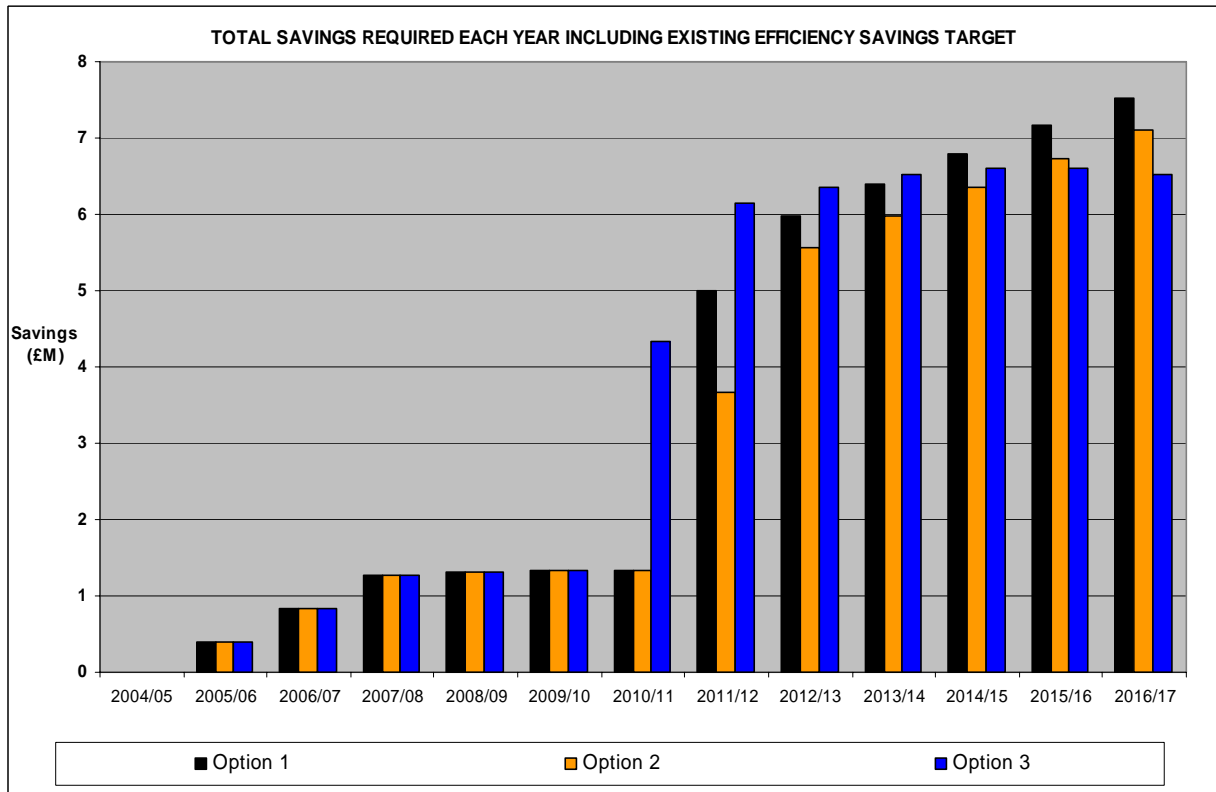
9.4 Option 1 will be most easy to communicate to taxpayers as it continues the £12 a year increase but is more prone to capping and requires the largest eventual reductions (£6.2M).

9.5 Option 2 is only marginally different to Option 1, will require slightly less reductions (£5.8M) savings but the concept of retrieving this years repayment will need to be explained. It is the most prone to capping but only slightly more so than Option 1.

9.6 Option 3 requires least service reductions (£5.2M), is least prone to capping and would be recognised as attempting to follow the Government’s approach. It does however result in smaller tax increases now but larger ones in due course. The graph below illustrates this point.



9.7 The following graph shows the total savings required each year including the efficiency target already included in the MTP.



9.8 **Cabinet is invited to consider the information outlined above and ask the Overview and Scrutiny Panel (Planning and Finance) for its comments. Cabinet will then have the opportunity to debate its recommendation to Council at the meeting on the 15 September.**

9.9 To allow the review of the Medium Term Plan to progress the recommendations will need to include:

- The preferred option
- Whether the assumed continuation of a small capital programme beyond 2009/10 is acceptable.

**ACCESS TO INFORMATION ACT 1985**

Source Documents:

1. Working papers in Financial Services
2. 2005/06 Revenue Budget and the 2005/010 MTP

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## ANNEX A

OPTION 1	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000
Efficiency savings target already included	0	-402	-826	-1,273	-1,307	-1,342	-1,342	-1,342	-1,342	-1,342	-1,342	-1,342	-1,342
<b>2005/06 BUDGET/MTP/Forecast</b>	<b>16,685</b>	<b>17,373</b>	<b>18,844</b>	<b>19,476</b>	<b>21,122</b>	<b>22,774</b>	<b>24,366</b>	<b>25,542</b>	<b>26,617</b>	<b>27,717</b>	<b>28,817</b>	<b>29,917</b>	<b>31,017</b>
Rebiling	0	60	0	0	0	0	0	0	0	0	0	0	0
Revenue/capital adjustment	-315	-169	0	0	0	0	0	0	0	0	0	0	0
2004/05 outturn	-1,557	292	0	0	0	0	0	0	0	0	0	0	0
Inflation adjustment	0	70	224	312	405	503	606	714	828	948	1,074	1,207	1,346
<b>Additional required savings</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>-3,666</b>	<b>-4,644</b>	<b>-5,050</b>	<b>-5,443</b>	<b>-5,823</b>	<b>-6,189</b>
Funding capital expenditure	0	0	0	0	0	0	0	81	367	677	990	1,306	1,625
Interest adjustment	-257	-459	-443	-71	-57	-62	-31	-52	-4	-10	-16	-22	-28
<b>2006/07 BUDGET/MTP/Forecast</b>	<b>14,556</b>	<b>17,167</b>	<b>18,625</b>	<b>19,716</b>	<b>21,470</b>	<b>23,215</b>	<b>24,941</b>	<b>22,619</b>	<b>23,164</b>	<b>24,282</b>	<b>25,423</b>	<b>26,585</b>	<b>27,771</b>
% increase		17.9%	8.5%	5.9%	8.9%	8.1%	7.4%	-9.3%	2.4%	4.8%	4.7%	4.6%	4.5%
<b>FUNDING</b>													
Government support	-8,731	-9,508	-9,995	-10,481	-10,972	-11,219	-11,471	-11,730	-11,994	-12,263	-12,539	-12,821	-13,110
Collection fund deficit	14	4	0	0	0	0	0	0	0	0	0	0	0
Council tax	-5,308	-5,655	-6,399	-7,157	-7,929	-8,717	-9,519	-10,337	-11,170	-12,018	-12,883	-13,763	-14,660
<b>USE OF REVENUE RESERVES</b>	<b>531</b>	<b>2,008</b>	<b>2,231</b>	<b>2,079</b>	<b>2,569</b>	<b>3,278</b>	<b>3,951</b>	<b>553</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>COUNCIL TAX</b>	<b>£94.54</b>	<b>£99.71</b>	<b>£111.71</b>	<b>£123.71</b>	<b>£135.71</b>	<b>£147.71</b>	<b>£159.71</b>	<b>£171.71</b>	<b>£183.71</b>	<b>£195.71</b>	<b>£207.71</b>	<b>£219.71</b>	<b>£231.71</b>
% Increase	14.5%	5.5%	12.0%	10.7%	9.7%	8.8%	8.1%	7.5%	7.0%	6.5%	6.1%	5.8%	5.5%
Revenue reserves End of year	18,669	16,661	14,430	12,351	9,782	6,504	2,553	2,000	2,000	2,000	2,000	2,000	2,000
Capital reserves End of year	49,861	35,242	16,829	13,879	9,852	4,634	968	0	0	0	0	0	0

