CABINET **6 SEPTEMBER 2007**

FINANCIAL FORECAST
(Report by the Head of Financial Services)

1 PURPOSE

1.1 This report considers the Financial Forecast for the next 10 years and highlights the major uncertainty that will exist until the Government's draft grant figures are received in December.

1.2 This report will be considered by the Overview and Scrutiny Panel (Corporate and Strategic Framework) on 4 September and Cabinet will then have the opportunity to consider their comments on 6 September prior to making their own recommendations to Council (26 September).

2 BACKGROUND

2.1 The Comprehensive Spending Review 2007 (CSR07) is expected to set out central government funding to local government for the next 3 years. This is expected to be announced prior to the Council setting its budget for 2008/9, but is not likely to be available until December.

2.2 The Council has continued to spend carefully and this, together with extra grants and buoyant income, resulted in last year's outturn being £2.7m less than budgeted, though £0.4m of this will be needed to fund projects unavoidably delayed. This has been added to Revenue Reserves giving a total of £19.5m at April 2007. Capital reserves amount to £28.7m and capital expenditure of £0.8m has been brought forward.

2.3 Our existing financial strategy recognises that we will have a number of years with deficits funded from reserves before equilibrium can be achieved. It also recognises that finding additional income, specific grant funding or savings to achieve this total will be a challenge.

3. FUNDING

3.1 The Councils net revenue expenditure has to be funded from government general grant, council tax and reserves. The table below indicates the scale by which total funding could vary from the current plan. The following sections then provide further information on each of the three elements:

FUNDING	07/08 £M	08/09 £M	09/10 £M	10/11 £M	11/12 £M	12/13 £M	13/14 £M	14/15 £M	15/16 £M	16/17 £M	17/18 £M
Current Approved Plan											
Government Grant	11.7	12.2	12.7	13.0	13.4	13.8	14.1	14.5	14.9	15.3	15.8
Council Tax	6.3	6.7	7.1	7.8	8.5	9.2	9.9	10.8	11.6	12.5	13.5
Reserves	1.6	2.0	2.7	2.9	2.2	1.5	0.8	0.5	0.4	0.4	0.2
	19.5	**20.8**	**22.5**	**23.7**	**24.1**	**24.5**	**24.9**	**25.8**	**27.0**	**28.3**	**29.4**
Best (?) Scenario											
Government Grant	11.7	12.0	12.3	12.5	12.6	12.7	12.9	13.0	13.2	13.4	13.5
Council Tax	6.3	6.7	7.1	7.8	8.5	9.2	9.9	10.8	11.6	12.5	13.5
Reserves	1.6	2.0	2.7	2.9	2.2	1.5	0.8	0.5	0.4	0.4	0.2
	19.5	**20.7**	**22.1**	**23.2**	**23.3**	**23.4**	**23.6**	**24.3**	**25.2**	**26.3**	**27.2**
Possible Scenario											
Government Grant	11.7	11.9	12.1	12.1	12.2	12.2	12.3	12.4	12.5	12.5	12.6
Council Tax	6.3	6.7	7.0	7.4	7.8	8.3	8.7	9.2	9.7	10.2	10.8
Reserves	1.6	2.0	2.7	2.9	2.2	1.5	0.8	0.5	0.4	0.4	0.2
	19.5	**20.6**	**21.8**	**22.4**	**22.2**	**22.0**	**21.8**	**22.1**	**22.6**	**23.1**	**23.6**
Worst (?) Scenario											
Government Grant	11.7	11.6	11.1	10.7	10.8	10.8	10.9	11.0	11.0	11.1	11.2
Council Tax	6.3	6.7	7.0	7.4	7.8	8.3	8.7	9.2	9.7	10.2	10.8
Reserves	1.6	2.0	2.7	2.9	2.2	1.5	0.8	0.5	0.4	0.4	0.2
	19.5	**20.3**	**20.8**	**21.0**	**20.8**	**20.6**	**20.4**	**20.7**	**21.1**	**21.7**	**22.2**

4 GOVERNMENT GENERAL GRANT

4.1 In December 2005 the Government, for the first time, announced two year's grant. They gave a definite figure for 2006/7 and a clear indication for 2007/08 which they subsequently did not alter. This was the first stage in moving to three year announcements with the first due this December to cover 2008/09, 2009/10 and 2010/11. This is integrated with the Government's own three yearly spending review (CSR07).

4.2 Whilst this will give councils a much better basis on which to make their shorter term plans it will unfortunately result in major volatility every three years, rather than smaller variation each year. This volatility has two main elements – the total amount the Government is prepared to distribute to local government and changes to the formula by which this total sum is allocated to individual councils.

4.3 The starting point for the amount to be allocated is to identify any changes in responsibilities that councils will have in the coming 3 years. The Government then adds to the total their assessment of what the extra cost will be but, unfortunately, there are often major differences of opinion on whether their assessment is reasonable. Then the Government will add an allowance for inflation but, again, councils often consider that this is not realistic. Finally there have been a number of rumours that suggest the total sum will then be reduced by anything up to 5% per year for assumed cashable efficiency improvements.

4.4 The Government has also produced a consultation document on potential changes to the allocation formula. There are three elements of particular interest:

- Concessionary Fares
- Area Cost Adjustment
- Tapering of Changes (Floors)

4.5 Concessionary Fares

The Government introduced the requirement for free passes and free travel within council boundaries to be introduced in April 2006 and added some extra funding to meet the cost. Unfortunately there was no way to accurately forecast the costs for councils in advance and it is still not clear on a national scale whether the addition was adequate. Huntingdonshire decided, along with the other Cambridgeshire Authorities, to introduce an enhanced scheme that provided free travel within the County boundary rather than just within the District boundary. The County Council agreed to a safety net arrangement whereby any costs over an agreed level would be funded from the Huntingdonshire share of the LPSA reward funding in 2006/07 and 2007/08.

From April next year the Government are extending the scheme to provide free national bus (not coach) travel and are adding a further amount to their financial support to fund this. Again, due to the bus companies being entitled by the legislation to recover their actual additional costs, rather than a pre-negotiated sum, there is no certainty of what an individual council's extra cost will be, much less the national total.

The basis of charge to individual council's is also altering with the charge for each single journey falling on the council in whose area that journey starts rather than on the Council that issued the pass.

The Government have not yet decided whether the funding will be via a specific grant or will be included in the general grant, but have anyway included some options for how it is allocated based on a national total of £200m. The impact on Huntingdonshire ranges from an increase of £223k to £375k.

The current financial plan assumes that any costs in excess of £468k will from April be met from this extra grant.

4.6 Area Cost Adjustment

Some years ago, following many years of lobbying, the Government recognised that costs were higher in Cambridgeshire than many areas of the country and so the grant formula was adjusted to reflect this. They are now suggesting that this should only have been applied to Cambridge City, South Cambridgeshire and the County Council because the other Cambridgeshire councils have lower pay levels. If this adjustment is made then Huntingdonshire will lose £465k per year in government support.

4.7 Tapering of Changes

The Government does not wish councils who lose grant because of changes to the formula to have to suddenly reduce spending all in one year. It therefore introduced a system whereby those councils that were due to have increases in grant had them temporarily reduced so that those councils that were due reductions had a bit longer before their whole reduction was made. This led to Huntingdonshire still being owed £364k in grant from when the area cost adjustment was made. The current consultation provides options for reducing this tapering, based on a council being only protected at 0%, 1% or 2% in CASH terms. Any tapering would not work with an annual efficiency savings adjustment and so it is assumed it would only relate to formula changes, such as removal of the area cost adjustment.

4.8 Overall Impact

Obviously it is impossible to forecast the impact of such significant grant volatility but three scenarios are illustrated to give an idea of the scale of the uncertainty.

Best (?) Scenario

Inflation 2.75%, 1.5% efficiency savings reduction, no change to area cost adjustment, no change to tapering, amount given for Concessionary fares (say £375k) matches costs.

Possible Scenario

Inflation 2.75%, 2.5% efficiency savings reductions for 3 years and then 2% thereafter, no change to area cost adjustment, no change to tapering, amount given for Concessionary fares (say £375k) matches costs.

Worst (?) Scenario

Inflation 2.75%, 5% efficiency savings reductions for 3 years and then 2% thereafter, area cost adjustment removed (£465k), tapering on £465k only, amount given for Concessionary fares (say £223k) is £152k less than costs.

GRANT FUNDING	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
Current Approved Plan	£M	£M	£M	£M	£M	£M
True grant forecast	12.0	12.3	12.7	13.0	13.4	13.8
Less withheld for tapering	-.4	-.2	0	0	0	0
Current Approved Plan	**11.7**	**12.2**	**12.7**	**13.0**	**13.4**	**13.8**
Best (?) Scenario						
True grant forecast		12.5	12.7	12.9	13.0	13.2
Less withheld for tapering		-.2				
Less Concessionary Fares increased cost		-0.4	-0.4	-0.4	-0.4	-0.4
Net Position		**12.0**	**12.3**	**12.5**	**12.6**	**12.7**
LOSS compared with Current Plan		**-0.2**	**-0.4**	**-0.6**	**-0.8**	**-1.0**
Possible Scenario						
True grant forecast		12.4	12.5	12.5	12.6	12.6
Less withheld for tapering		-.2				
Less Concessionary Fares increased cost		-0.4	-0.4	-0.4	-0.4	-0.4
Net Position		**11.9**	**12.1**	**12.1**	**12.2**	**12.2**
LOSS compared with Current Plan		**-0.3**	**-0.6**	**-1.0**	**-1.2**	**-1.5**
Worst (?) Scenario						
True grant forecast	-	11.7	11.4	11.1	11.2	11.3
Tapering protection on area cost adjustment		0.3	0.2			
Less Concessionary Fares increased cost		-0.4	-0.4	-0.4	-0.4	-0.4
Net Position		**11.6**	**11.1**	**10.7**	**10.8**	**10.8**
LOSS compared with Current Plan		**-0.6**	**-1.5**	**-2.3**	**-2.6**	**-2.9**

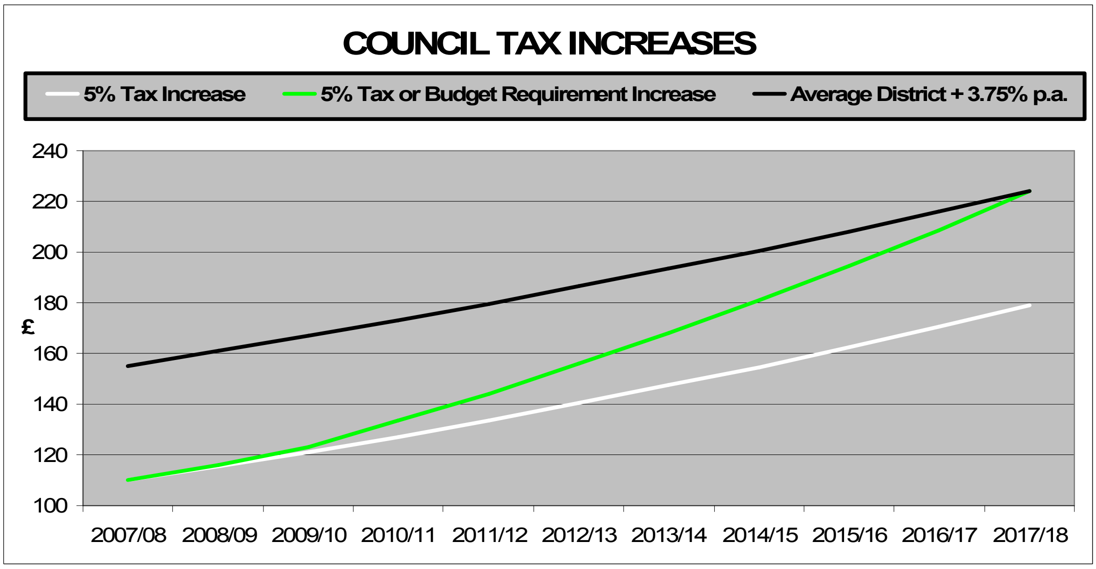
5. COUNCIL TAX

5.1 All scenarios assume the tax base will continue to grow by 0.5% per year, as there are no significant indications to the contrary.

5.2 The **Best Scenario** assumes that the Government will maintain the dual element to its capping regime that it has to date (i.e. that both Council Tax and budget requirement increases have to exceed 5%) and the Council continues to be comfortable with Council Tax increases in excess of 5%.

5.3 The **other scenarios** assume either that the Government changes the targets such that no more than a 5% tax increase is permitted or the Council resolves that a Council Tax rise of 5% is sufficient.

5.4 The graph below shows the two scenarios and the current average District Council Tax increasing by 3.75% per annum.



6. USE OF RESERVES

6.1 The current approved Forecast is based on allowing Revenue Reserves to fall to £2.1m and then to be retained at that level as shown in the following table. In order to simplify a very complex set of inter-relationships **all Scenarios** are based on this use of reserves.

RESERVES	07/08	08/09	09/10	10/11	11/12	12/13	13/14	14/15	15/16	16/17	17/18
	£M	£M	£M	£M	£M	£M	£M	£M	£M	£M	£M
Use of Revenue Reserves	1.6	2.0	2.7	2.9	2.2	1.5	0.8	0.5	0.4	0.4	0.2
Remaining Reserves at end of year	15.6	13.7	11.0	8.1	5.9	4.4	3.5	3.1	2.6	2.3	2.1

7. NET EXPENDITURE

7.1 The items affecting net expenditure at this stage are:

- Inflation: General inflation, pay inflation and assumed increases in fees and charges
- Interest Rates
- Minimum level of revenue reserves
- Service Changes 2006 to March 2011
- Service Variations post April 2011
- Other significant items.

7.2 Inflation

General inflation continues to be based on 2.5% but 5% has been included for fuel prices.

Pay inflation continues to run ahead of general inflation. This recognises increased standards of living and efficiency and is particularly noticeable locally because of the general business growth and affluence of the Cambridge sub-region. There are also national, and more local, shortages of key types of staff with authorities, inevitably, in the shorter term having to “outbid” each other to maintain service delivery. This is further exacerbated by increased demand for certain professions from the private sector and other organisations. It is therefore considered necessary to continue to allow for 3% pay inflation and to revert to making full allowance for average levels of performance pay as there is now so much less opportunity to achieve reduced pay levels when staff leave.

Pension costs are based on the actuary’s requirements up to 2010/11 but it is anticipated that the results of the latest three-yearly review will be available before the budget is finalised. Recent indications had suggested further increases would be minimal but it must be appreciated that the figures are closely linked, in part, to the performance of the equity market, which is again volatile.

7.3 Interest Rates

Forecasting future interest rates continues to be a challenge. It has been assumed that we will earn 5.4% on our investments this year, 5.75% in 2008/09, 5.5% in 2009/10 and 5% thereafter. This will be reviewed at each stage of the budget process. The Interest rate for borrowing has been assumed at 4.6%.

7.4 Service Variations 2007 to March 2012

Previously planned changes in budgets (MTP schemes) have been reflected in the financial forecast.

7.5 Service Variations post March 2012

It is necessary to consider what general provision for service variations should be made beyond the level to March 2012 agreed in the MTP.

It has been assumed that, given the financial position the Council will be facing in the coming years, any additional revenue developments should be funded from compensating savings or additional specific grant or contributions.

£3.8m per year for capital investment (at current prices) has been included and this would be sufficient **for example** to fund:

	£000
Social Housing Grant	1,000
Leisure Centre Maintenance (300) and regular replacement of fitness equipment (200)	500
Disabled Facilities Grants	900
Vehicle Replacements	600
Other items	800
	3,800

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 additional savings.

7.6 Revenue Reserves

The Council must have sufficient reserves to meet any unexpected difficulties without facing the disruption of having to temporarily cut services until it can increase the following year's Council Tax or make alternative service cuts. The actual level is a matter for detailed analysis as they fall towards that level but it is felt that £2.1m is probably now too low especially with the new expected periodic volatility in Government Grant.

It has been assumed, just for the modelling in this report, that the extra £2.7m resulting from last year's outturn will be added to this minimum level. This will be reviewed for the November report and part of this sum is then likely to be used to provide time to achieve efficiency savings.

7.7 Other significant items

There are no other items that have emerged from last year's outturn and/or the current years monitoring that are significant enough to be included in the forecast at this time.

7.8 Items not taken account of

There are also some items that it is not possible to take account of at this stage but which may need to be brought into the MTP before it is approved next February if additional information becomes available in time. These include:

- The VAT position on off-street car parking which is the subject of continuing judgements and appeals. If it is finally resolved in favour of local authorities there will be a benefit of £150k per year.

- Potential service developments not already in the MTP and any unavoidable spending requirements.

- The Council was extremely successful in achieving additional grant funding last year. Whilst this is extremely difficult to forecast with any certainty it is likely that additional sums of LABGI and other grants will be obtained.

- Any concessionary fares costs in excess of £468k that are not covered by additional Government Grant.

- There may be a significant loss of income on Land Charges due to increased volumes of Personal Searches.

- There may be additional income from car park fees depending on the decisions taken on the recommendations from the Car Parking Working Party.

7.12 Resulting impact on net spending

The table below compares the revised forecast of net spending compared with the approved plan and highlights the variation.

NET SPENDING FORECAST	07/08 £M	08/09 £M	09/10 £M	10/11 £M	11/12 £M	12/13 £M	13/14 £M	14/15 £M	15/16 £M	16/17 £M	17/18 £M
Approved Plan	19.5	20.8	22.5	23.7	24.1	24.5	24.9	25.8	27.0	28.3	29.4
Revised position	19.4	20.5	22.6	24.4	25.0	25.9	26.8	28.0	29.7	31.5	33.0
Variation	**-0.2**	**-0.3**	**0.1**	**0.7**	**1.0**	**1.4**	**1.9**	**2.2**	**2.7**	**3.2**	**3.6**

8. SPENDING ADJUSTMENTS

8.1 Heads of Service have produced draft 5 year visions for their services that identify key priorities for additional spending (if the funding can be found) and opportunities for reducing spending. These are being discussed with Directors and refined so that relevant items can be incorporated into the draft budget/MTP stage of the process in November.

8.2 Particular emphasis is being placed on identifying opportunities for:

- increasing specific grant funding and contributions from other bodies (e.g. LABGI, Planning Delivery Grant, LAA reward grant)
- investment opportunities that provide a net surplus
- efficiency savings
- deleting any budget sums no longer required (as illustrated by last and previous years' underspending)
- increasing fees and charges

It is anticipated that these will allow the already required savings targets to be achieved.

8.3 Any level of lost funding emerging from section 3 above and the variations in net spending shown in paragraph 7.12 will have to be met from further such spending adjustments. There is still likely to be sufficient flexibility provided by revenue reserves to achieve this in an organised manner.

9 SENSITIVITY AND RISKS

9.1 The Financial Forecast takes a longer-term view and, within that time frame, many of its assumptions will turn out to be inaccurate and for this reason a sensitivity analysis is usually performed to identify the potential impact if any of the key assumptions change. Due to the major uncertainty on Government Grant that will be resolved in December there is limited value in carrying out this exercise until January when it will be included in the final stage of the budget and Council Tax setting.

10 CONCLUSIONS

10.1 The benefits to forward planning, from certainty on grant figures for three years, appear to be illusory if the current major uncertainty on grant levels is to be repeated every three years. It is impossible to forecast what the change will be in Government Grant at this stage but it could easily be significant.

10.2 There will be unavoidable additional spending from the inflation and other adjustments included in this report and there may well be other unavoidable areas of spending which will emerge during the budget/MTP process.

10.3 The Council continues to be successful in identifying revenue savings and additional grant funding. This together with the emerging proposals from services' five year visions will allow significant options to be identified for reducing spending levels. Visions will also help to prioritise proposals for service developments within any available funds.

10.4 Cabinet will have the comments from the Overview & Scrutiny Committee available when they consider this report.

11 RECOMMENDATIONS

11.1 Cabinet is recommended to:

i) note this report

ii) highlight to Council

- the past successes in controlling spending and obtaining additional grant funding which will form important elements for reducing future spending
- the development of the 5 year visions which will create additional spending reductions and help prioritise proposals for service developments
- the major uncertainty over future grant levels and the consequent inability to create reasonable plans until the 3 year grant levels are known in December.

ACCESS TO INFORMATION ACT 1985

Source Documents:

1. Working papers in Financial Services
2. 2006/07 Outturn, 2007/8 Revenue Budget and the 2008/2012 MTP

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