Harrow COUNCIL LONDON

REPORT FOR: CABINET

Date of Meeting:	11 July 2019
Subject:	2 Year Budget Strategy – 2020/21 to 2021/22
Key Decision:	Yes
Responsible Officer:	Sean Harriss, Chief Executive Dawn Calvert, Director of Finance
Portfolio Holder:	Councillor Graham Henson, Leader of the Council Councillor Adam Swersky, Portfolio Holder for Finance and Resources
Exempt:	No
Decision subject to Call-in:	Yes
Wards affected:	All
Enclosures:	None

Section 1 – Summary and Recommendations

This report sets out the Council's Budget Strategy over the 2 year period, 2020/21 to 2021/22.

Recommendation

Cabinet is asked to:

(a) Note the actions and options in Stage 1 and Stage 2 to reduce the 2020/21 to 2021/22 budget gap (paragraph 1.3.3)

(b) Note the key themes being explored to support the 2 year Budget Strategy 2020/21 to 2021/22 (paragraph 1.3.3)
(c) Recommend the addition of £100m to the Capital Programme, for long term commercial investment, to Council for approval (paragraph 5.5)
(d) Note the action to refresh the Investment Property Strategy and engage external professional advice to support the commercial investment (paragraph 5.6)

Reasons

(a) To ensure the Council manages within the challenging financial environment it faces and achieves financial sustainability over the medium term.

Section 2 – Report

1.1 Background

1.1.1 The Government continues to reduce its funding to Local Government as part of its nationwide austerity programme. In their publication 'Local Government Funding – Moving the conversation' (June 2018) the Local Government Association shared a number of their key statistics including:

- New analysis indicates that local services face a funding gap of £7.8 billion by 2025 of which £6.6 billion relates to Adult Social Care and Children's Services.

- By 2020, local authorities will have faced a reduction to core funding from Central Government of nearly £16 billion over the preceding decade.

1.1.2 This nationwide picture has translated itself into a budget gap of circa £128m for Harrow Council to manage over the 7 years, 2013/14 to 2019/20, as detailed in table 1 below:

Table 1: Summary of Key Financial Changes 2013/14 to 2019/20

	Reduction in RSG	Demand Led Growth	Technical Savings	Savings	Additional Revenue from Council Tax	Business Rates
	£'m	£'m	£'m	£'m	£'m	£'m
2013/14	52.1	10	10	-22	-1.8	14.7
2014/15	42.6	5.5	-2.1	-10	-1.9	14.5
2015/16	32	7.7	5.9	-20.6	-3.4	14
2016/17	21.9	4.7	9.5	-16.6	-6.8	13.2
2017/18	13	10.7	-0.6	-10.2	-7.3	14.4
2018/19	7.3	9.8	1.7	-7.4	-5.3	14.4
2019/20	1.6	7.4	-4	-5.2	-8.5	14.4
Total	**50.5**	**55.8**	**20.4**	**-92**	**-35**	

The table shows:

- The Council has seen the Revenue Support Grant, its main source of funding from central government, reduce by 97% over the 7 years, reducing the grant to £1.566m (£1.6m).

- Over and above the RSG, the Council receives no additional funding to meet demographic and inflationary pressures. Therefore growth of £55.8m has had to be provided to fund the continued pressures on front line services, mainly adults and children’s social care and homelessness. Technical growth of £20m has had to be provided to fund inflationary pressures (pay and non pay) and the cost of capital investment in initiatives including highways maintenance and the acquisition of properties to alleviate homelessness.

- These three factors have taken the total budget shortfall to find over the seven years to £128m to achieve a balanced budget.

- Savings and efficiencies of £92m have been achieved but the profiling of these savings, and how the quantum has reduced in recent years, demonstrates the challenges of finding sustainable savings year on year.

- Council Tax has been increased largely in line with referendum limits (2.99% in 18/19 and 19/20). In addition, Council Tax has been increased by an additional 5.5% over the three years 2017/18 to 2019/20 in respect of the Adult Social Care precept.

- Business Rates have remained largely static, the Borough has been adversely affected by permitted development allowing office space to be converted to residential and not benefitting from large areas of land available for business development.

The Council has received, and continues to receive one off funding, including:

- Transitional Grant (£712k in 2016/17 and £699k in 2017/18)
- Winter Pressures funding for Adults Social Care (£968k in 2018/19)
- Adult Social Care support grant (£606k in 2018/19)
- Adult and Children's Social Care (£2.627m in 2019/20)
- Improved Better Care Fund (£4.643m in 2018/19, £5.467m in 2019/20)
- London Business Rates Pilot Pool (£3.5m in 2019/20, £1.8m in 20/21)

Whilst this funding is well received the short term temporary nature of the income means that it can only be treat as a one off. The fact that it cannot be considered over the medium and long term does not assist the challenges of budget planning and achieving financial sustainability. (To note: The Improved Better Care Fund is built into the Medium Term Financial Strategy (MTFS) permanently. Due to the high value of the fund, assuming no funding in 2020/21 would create significant volatility to budget planning.)

1.1.3 Despite all reasonable actions, including council tax increases, significant savings, and efficiencies and generating income, it still remains a considerable challenge for the Council to balance its budget going forward in light of continued demand pressures facing the Council. In February 2019 full Council approved the Medium Term Financial Strategy (MTFS) 2019/20 to 2021/22. Despite achieving a balanced budget for 2019/20, there remains a budget gap of £26.140m for 2020/21 and 2021/22.

1.1.4 Harrow Council does not have large cash reserves. Its General Fund balances stand at £10m and remain within the lower quartile when benchmarked with other local authorities and the Council has consistently taken the view that spending them is not a responsible way to offset lost revenue. The Council does exercise robust financial management and has not overspent its revenue budget for the last 7 years. The Council has not shied away from implementing in year spending controls if early indications suggest a balanced budget positon is not on track. Such actions have helped to prevent a draw down on the Council's limited cash balances.

1.2 Future Uncertainty

1.2.1 The Council's drive for financial sustainability is not assisted by considerable uncertainty around funding and service direction:

- A Comprehensive Spending Review (CSR) and Fair Funding Review are planned for 2019/20. The CSR will set the overall quantum of central government funding to local government and the Fair Funding Review will reset the needs base line which will determine how the overall quantum is distributed. There is much speculation that the ongoing negotiations on Brexit will adversely impact upon the timings of the CSR and Fair Funding and the most likely scenario is that the Council's 2020/21 funding settlement will be a roll forward from 2019/20. This situation does nothing to address the low funding baseline for the Council. In 2019/20 the Council's core spending power per head was estimated to be £170 lower that the London average and £75 lower than the rest of England average.

- The Adult Social Care Green paper has been subject to many delays. As people are living longer and the population ages Central Government recognises the need to reach a long term sustainable solution to providing the care older people need. A confirmed date for the release of the green paper remains unknown and the Council remains subject to temporary injections of funding, which whilst appreciated, cannot be used to underpin longer term planning and decision making.

- Business Rates are currently subject to reform with central government intending to allow local government, as a whole, to retain all or a significant proportion of its rates collected. Prior to 2018/19 Councils retained 30% of their business rates collected. From 2018/19 Harrow has been part of the London Business Rates Pool allowing the council to receive a proportion of the collective growth in London. Initially the pool was for 1 year only but has been extended for a second. The Council has benefitted financially from the pool (£5.4m in 2018/19 and an estimated £1.8m in 2019/20). However once again the funding is temporary and not confirmed until after the end of the financial year to which it relates making it difficult to build into longer term planning.

- Schools are funded by the ring fenced Dedicated Schools Grant (DSG) which sits outside of the General Fund. Within the DSG is the High Needs Block (HNB) which funds provision for pupils with high needs placed in special schools and special provision in mainstream schools in Harrow and out of Borough. A recent survey showed that London Borough's had a total shortfall of £78m in 2017/18 compared with high needs allocations with many now estimating having to apply reserves to meet the pressures. In December 2018 central government announced additional funding for local authorities with Harrow receiving £606k for both 2018/19 and 2019/20. Despite this support for the first time Harrow has had to set a £3.3m deficit budget for its HNB in 2019/20 and future central government support is unknown at this point.

1.3 2 Year Budget Strategy 2020/21 to 2021/22

The Strategy

1.3.1 To meet its statutory requirements, the Council must set a balanced revenue budget for the forthcoming financial year. It is essential to look to the medium term and the council also produce's a 3 year MTFS which is refreshed annually. Funding uncertainties make it increasingly difficult to set a balanced budget over the medium term when what is going to happen from one year to the next remains largely unknown. The Council's current 3 years MTFS identifies a budget gap of £26.140m for year 2 and 3. Looking forward this budget gap will not be addressed on an annual basis (£16.795m in 2020/21 and £9.3m in 2021/22) but as a two year strategy to ensure:

- Those plans / initiatives that require less lead in time can be realised as early as possible in the process
- This will provide space for those plans / initiatives requiring a longer lead in time to be fully worked through, including consultation and equality impact assessment, before final inclusion in the MTFS
- A robust plan for the use of reserves specifically ear marked to support the 2 year strategy

1.3.2 The over arching principle underlining the approach is to develop stages which exhaust all opportunities to reduce expenditure and or generate income to protect frontline services from impact, a reduction of which is considered a last resort. If the strategy does not achieve sustainability, the last resort savings could potentially include further library closures, higher caseloads for spcial workers, lower frequencies of street cleaning and reductions in early intervention and preventative services.

1.3.3 Clearing the budget gap solely through increasing Council Tax would require an increase of circa 20%. Since setting the final budget and MTFS in February of this year there has been focused attention on managing the budget gap and associated risks. These will be explained in three stages:

Stage 1 – Reducing the quantum of the budget gap
Stage 2 – Options on future Council Tax increases
Stage 3 - A 2 year budget strategy based on 4 key themes

Stage 1 – Reducing the quantum of the budget gap

The identified budget gap of £26.140m can be reduced to £21.1m by:

- Evidence based assumptions on future increases in the Council Tax base (increase in the number of band D equivalent properties) not currently built into the MTFS
- Maintaining high collection rates for Council Tax and Business Rates
- Income realisation from the letting of the 53 units at Gayton Road for market rent
- Assuming Council Tax will be increased at the referendum level of 1.99% in 2021/22 which is not built into the current MTFS

The uncertainties described in this report could potentially impact on the quantum of the budget gap, either in a postive or negative way. The quantum of the budget gap remains under constant review.

Stage 2 – Options on future Council Tax Increases
Following stage 1, the MTFS assumes a Council Tax increase up to the referendum level of 1.99% in 2020/21 and 2021/22. A 1% increase in Council Tax generates approximately £1.250m. In recent years central government has allowed councils flexibility in terms of increasing annual rates without requiring a referendum:

- Adult Social Care Precept – over the three years up to 2019/20 the flexiiblity to increase Council Tax by a maximum of 6%. Harrow levied 5.5%.

- Additonal 1% Council Tax (over and above the core increase of 1.99%) in 2018/19 and 2019/20 which Harrow applied in full.

The understanding is that the fiscal calculations of central government assume an increase in Council Tax of 5% per annum for the next two years. For Harrow this would generate approximately £7.5m in on going revenue to support core services hence reducing the budget gap to £13.6m. The Administration can make a choice on what it does in respect of Council Tax increases moving froward. Central Government announcements on Council Tax are normally received in November or December around the time of the provisional local government financial settlement.

Stage 3 – A 2 Year Budget Strategy based on 4 key themes
Following stage 2, the budget gap has the potential to be reduced to £13.6m. In terms of the 2 year budget strategy this has been rounded up to £15m to provide for an element of choice.

The over arching principle underlining the strategy is to develop themes which exhaust all opportunities to reduce expenditure and or generate income to protect frontline services from impact. The strategy is centered on 4 key themes:

- Corporate and Technical (£2m to £4m)
- Commercial Investment and Income (£2m to £3m)
- Service Efficiency and Savings (£2m to £3m)
- Transformation Programme (£3m to £5m)

Corporate and Technical (£2m to £4m)
This theme will review all corporate budgets (for example inflation, specific provisions and pan organsation expenditure) with a view to achieving efficiencies. The Councils treasury management function will be reviewed to ensure activities are done at the most optimum cost / return for the Council. Due to its nature, this theme is likely to realise the majority of early savings and all opportunties, when worked through, will be reported and implemented immediately.

Long Term Commercial Investment and Income (£2m to £3m)
The Council has undertaken a limited number of Commercial investment opportunities to generate a net return to the general fund. In December 2015, the Council approved its Investment Property Strategy. Since 2015 the Council has purchased 4 investment opportunities costing £17m and generating an annual return in the budget. The Strategy will be reviewed and the opportunties for further commercial investments will be identified paying due regard to the statutory requirements of the Prudential Code, the Council's current exposure to debt and risk and mitigations.

The Council has achieved success at selling services to generate a return. Further opportunities will be explored paying attention to targets already built into the MTFS and the risk that income streams can be subject to volatility.

Service Efficiency and Savings (£2m to £3m)
Transformation Programme (£3m to £5m)
There is likely to be a considerable overlap between these two themes therefore they are considered together. The Transformation Plan is being put together on the basis of how to modernise the Council, introduce new technology and re-design how services and functions operate. Areas currently being explored included technology, digital access, how the Council works, people development and management and centralisation of services. These themes are in their infancy and will more than likely be the plans and initiatives that will require the longest lead in time.

<u>Resourcing Implications</u>

1.3.4 The delivery of the strategy is dependent upon:

- The delivery of the 2019/20 budget to ensure no adverse impact on future years.
- Holding sufficient financial resilience to mitigate the risks inherent in stages 1 and 2.
- Funding to support the 2 year Budget Strategy, especially the transformation elements to delivery future efficiencies
- Funding to support the budget if the 2 year strategy slips or there is an adverse impact outside of the Council's control.

1.3.5 The 2018/19 outturn report, that was presented to Cabinet in June, detailed a number of reserves (one off) that are ear marked to provide financial capacity to support the delivery of the budget strategy and to mitigate risk that is inherent in some of the assumptions being made to reduce the budget , especially assumptions around Council Tax:

- **Business Risk (GF Transformation Reserve) - £7.526m.** This reserve is ear marked to fund the risk around the assumption of being able to increase Council Tax by 5% per annum for the next two years (stage 2). If central government do not allow an increase over and above 1.99% or the Administration does not wish to increase to 5%, the reserve will provide temporary support to the budget whilst alterative proposals are being worked on. If the Council Tax is increased by 5% in either one or both years of the strategy, this ear marked reserve will not be required and can be applied elsewhere.

- **Budget Planning Reserve - £2.629m.** The reserve balance is £6.829m of which £4.2m is committed to the 2019/20 budget. The remaining balance of £2.629m is ear marked for 'budget smoothing'. For example if sufficient plans and initiatives are not identified to balance the 2020/21 budget, this reserve can be drawn down to achieve a balanced position. It is recognised that this is only a temporary solution and potentially pushes the gap into future years and this will be monitored very carefully. It also provides space for those initiatives requiring a longer lead in time to be developed.

- **Capacity Building Reserve - £4.261m.** A small balance of £261k is ear marked for previously agreed plans leaving £4m to support the transformation theme to deliver £3m to £5m per annum. Use of this funding will include growing capacity to deliver the strategy and transformation and investment in IT.

- **Commercialisation Reserve - £1.265m.** This has been boosted to support commercial risk.

1.3.6 The actions required to manage the budget gap need to be permanent reductions or income generation.

1.3 Options considered

1.3.1. This report has detailed a number of options to reduce the reported 2 year budget gap of £26.140m. The report introduces the key themes supporting the 2 Year Budget Strategy. As the work progresses on this strategy all suitable options will be explored with the results being reported to Cabinet as appropriate.

2. IMPLICATIONS OF THE RECOMMENDATIONS

2.1 Cabinet are being asked to note the actions and options to reduce the budget gap and the key themes supporting the 2 year Budget Strategy. Cabinet are being asked to recommend to Council the addition of £100m to the Capital Programme for long term commercial investments to generate a financial return. The details of which are detailed in the financial implications section.

3. PROCUREMENT IMPLICATIONS

3.1. There are no procurement implications arising from this report.

4. LEGAL IMPLICATIONS

4.1 Local authorities have broadly drawn powers allowing them to invest and to borrow, in each case either for purposes relevant to the performance of any of their functions or generally for the prudent management of their financial affairs (s1 and s12 of the Local Government Act 2003). They may also acquire property by agreement located either inside or outside of their borough for the purposes of any of their functions, including their investment functions, or otherwise for the benefit, improvement or development of their area (s120 of the Local Government Act 1972). Lastly, they may also take any action (whether or not involving the expenditure, borrowing or lending of money or the acquisition or disposal of any property or rights) which is calculated to facilitate, or is conducive or incidental to, the discharge of any of their functions, which would again include their investment functions (s111 of the Local Government Act 1972).
35.The council will need to ensure that in exercising its investment and borrowing functions to expand its property portfolio, that any actions are reasonable and proportionate and for proper purposes consistent with the Council's prudential regime and its investment strategy. Investment decisions also need to be taken mindful at all times the council's fiduciary duties to ensure the sound management of the public finances.

4.2 Legal due diligence will be required on all property acquisitions, to include a review of title and ownership, and searches and enquiries of the vendor, in order to ascertain relevant liabilities and restrictions connected with the subject property. The results of the legal enquiries, and any associated risks, should be considered prior to any decision to enter into contract.

4.3 On any sale of an investment property the Council will be required to obtain best consideration in accordance with s123 of the Local Government Act 1972. Usually this will be achieved by placing the property onto the open market or otherwise, in respect of a sale agreed off market, demonstrating by way of professional valuation that it is achieving no less than market value for the property.

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5. FINANCIAL IMPLICATIONS

5.1 The strategy to undertake long term commercial investments to generate a return to support core services will require capital funding from the Public Works Loans Board. In line with the Investment Property Strategy (December 2015 Cabinet) a gross yield of 7.5% must be achieved. After accounting for capital financing costs and other associated revenue costs a minimum net return of 1.75% will be generated.

5.2 Council borrowing falls within the Prudential Code. The framework established by the Code is to support local strategic planning, local asset management planning and proper option appraisal. The objectives of the Code are to ensure, within the framework, that the capital investment plans of Local Authorities are affordable, prudent and sustainable.

5.3 The Ministry of Housing, Communities and Local Government (MHCLG) issued statutory guidance on Local Government Investments issued under section 15(1) (a) of the Local Government Act 2003 effective from 1 April 2018. Within the guidance investments made by local authorities are classified into one of two main categories:

- Investments held for treasury management purposes
- Other investments

In respect of other investments, the guidance makes reference to proportionality and the extent to which funding service expenditure is dependent upon achieving the expected net profit. The returns from a long term commercial investment fund are being considered as one strand of a strategy to achieve financial sustainability, they are not being considered as the only strand. The council is required to disclose in its Capital Strategy (a new requirement from 01 April 2019) its exposure to commercial investment. The Council's Capital Strategy, approved by Council in February 2019, set out the Council's previous 4 commercial investments and updates to the Capital Strategy will include new investments.

5.4 Paying due regard to the Code and current debt levels (£446m as at June 2019) a long term commercial investment allocation of £100m is considered prudent and proportionate and will not over expose the Council to commercial risk. Based on a net return of 1.75% this will deliver an income stream of £1.75m per annum to support core services. By increasing long term commercial investments by £100m, the net revenue contribution from such activities increases to just under 2% of the Council's revenue budget which is still considered proportionate.

5.5 In accordance with Financial Regulations, this report requests that Cabinet recommend to Council for approval to add £100m to the Capital Programme. The additional £100m will be added to the Capital Programme on a cost neutral basis, ie. The cost of capital financing is equal to the revenue return generated hence cost neutral on the revenue budget. The estimated income stream of £1.75m will be added to the revenue budget during the annual refresh process prior to the draft budget being brought to Cabinet in December.

5.6 To support the long term commercial investment fund the current Investment Property Strategy will be refreshed and external professional investment advice will be engaged to support the refresh, the identification and subsequent management of commercial investments entered into. The cost of this external support will be procured in line with Contract Procedure Rules and initial costs will be funded from the Commercialisation Reserve.

5.7 If further actions identified to support the budget gap require a separate Cabinet decision, such decisions will be brought as timely as possible. Otherwise all actions will be built into the draft budget and MTFS brought to Cabinet in December.

6. PERFORMANCE ISSUES

6.1 The first reporting of financial performance against the 2019/20 budget is a separate report elsewhere on this agenda. A savings target of £5.946m is included in the 19/20 budget. As at the end of P2 (May) 46% of savings are rated green, 46% amber and only 8% as red. The majority of the amber savings relate to social care savings. Plans are in place but it is very early on in the financial year to assess if plans are delivering as expected. Performance will be tracked monthly. Due to a history of delivering a balanced budget and not shying away from implementing in-year spending controls if performance is not on track, no unmanageable adverse impacts from 2019/20 are expected into 2020/21 at this stage.

7. ENVIRONMENTAL IMPACT

7.1 There are no direct environmental impacts.

8. RISK MANAGEMENT IMPLICATIONS

8.1 The 2 Year Budget Strategy is based on 4 key themes to help mitigate the risk if one theme does not deliver as currently estimated.

8.2 Budget management is included on the Corporate Risk Register incorporated into the risk 'inability to deliver the Council's MTFS leading to a dereliction of duties resulting in government intervention / an inability to pay Council debts.'' As at Qtr 1 2019/20 the risk was rated as C2 – medium likelihood / critical impact. The Corporate Risk Register is updated quarterly.

9. EQUALITIES IMPLICATIONS/PUBLIC SECTOR EQUALITY DUTY

9.1 Decision makers should have due regard to the public sector equality duty in making their decisions. The equalities duties are continuing duties they are not duties to secure a particular outcome. The equalities impact will be revisited on each of the proposals as they are developed. Consideration of the duties should precede the decision. It is important that Cabinet has regard to the statutory grounds in the light of all available material such as consultation responses. The statutory grounds of the public sector equality duty are found at section 149 of the Equality Act 2010 and are as follows:

A public authority must, in the exercise of its functions, have due regard to the need to:

(a) eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under this Act;

(b) advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it;

(c) Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

Having due regard to the need to advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it involves having due regard, in particular, to the need to:

(a) remove or minimise disadvantages suffered by persons who share a relevant protected characteristic that are connected to that characteristic;

(b) take steps to meet the needs of persons who share a relevant protected characteristic that are different from the needs of persons who do not share it;

(c) Encourage persons who share a relevant protected characteristic to participate in public life or in any other activity in which participation by such persons is disproportionately low.

The steps involved in meeting the needs of disabled persons that are different from the needs of persons who are not disabled include, in particular, steps to take account of disabled persons' disabilities.

Having due regard to the need to foster good relations between persons who share a relevant protected characteristic and persons who do not share it involves having due regard, in particular, to the need to:

(a) Tackle prejudice, and

(b) Promote understanding.

Compliance with the duties in this section may involve treating some persons more favourably than others; but that is not to be taken as permitting conduct that would otherwise be prohibited by or under this Act. The relevant protected characteristics are:

- Age
- Disability
- Gender reassignment
- Pregnancy and maternity
- Race,
- Religion or belief
- Sex
- Sexual orientation
- Marriage and Civil partnership

9.2 There is no direct equalities impact.

10. CORPORATE PRIORITIES

The Council's vision 'Working Together to Make a Difference for Harrow' is supported by five priorities:

- Building A Better Harrow
- Supporting Those In Need
- Protecting Vital Public Services
- Delivering A Strong Local Economy For All
- Modernising Harrow Council

Section 3 - Statutory Officer Clearance

Name: Dawn Calvert Date: 01 July 2019	X	Chief Financial Officer
Name: Jessica Farmer Date: 01 July 2019	✓	on behalf of the * Monitoring Officer

Name: Nimesh Mehta Date: 28 May 2019	X	Head of Procurement

Name: Charlie Stewart Date: 01 July 2019	X	Corporate Director - Resources
Ward Councillors notified:		**No**
EqIA carried out: **EqIA cleared by:**		**No** **N/A**

Section 4 - Contact Details and Background Papers

Contact: Dawn Calvert - Director of Finance,
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Background Papers: none

Call-In Waived by the Chair of Overview and Scrutiny Committee	**NO**