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Report of the Deputy Chief Executive

Report to Executive Board

Date: 9th October 2013

Subject: Medium Term Financial Strategy 2014/15 to 2015/16

Are specific electoral Wards affected? If relevant, name(s) of Ward(s):	☐ Yes	☒ No
Are there implications for equality and diversity and cohesion and integration?	☐ Yes	☒ No
Is the decision eligible for Call-In?	☒ Yes	☐ No
Does the report contain confidential or exempt information? If relevant, Access to Information Procedure Rule number: Appendix number:	☐ Yes	☒ No

Summary of main issues

1. The purpose of this report is to update Members on the development of the Council's Medium Term Financial Strategy which is designed to deliver the Council's 'Best Council' ambition in the context of the Government's spending plans.

2. The Council to date has been successful in responding to the challenging reductions to its funding since 2010 which has been in the region of £94m over the past 3 years. Based on the national spending totals announced in the Spending Review, and a subsequent technical consultation, the Council now anticipates that there will be a further reduction in funding from Government of around £81m for core services over the two years 2014/15 and 2015/16. This reduction in funding is in addition to the need to meet the cost of inflation and continuing spending demands across a range of services.

3. The Medium Term Financial Strategy does not attempt to provide a detailed budget for the next two years but it does set out the main financial issues facing the Council and sets out a broad framework for the delivery of efficiencies and savings to bridge the identified funding gap. Initial budget proposals for 2014/15 will be brought to the December 2013 meeting of the Board.

Recommendation

4. Members are asked to approve the Medium Term Financial Strategy 2014/15 - 2015/16 and agree that the assumptions and principles outlined in this report will be used as a basis for the detailed preparation of the Initial Budget Proposals for 2014/15.

1. Purpose of report

1.1 This report sets out for the Board the principles and assumptions underlying the proposed financial strategy covering the years 2014/15 to 2015/16. This will provide the framework for the preparation of the 2014/15 initial budget proposals which will be presented to Members in December 2013.

2. Background information

2.1 The 2013 Spending Review published on 26th June 2013 set out the Government's spending plans for 2014/15 and 2015/16. Members received a report at the Executive Board meeting on 4th September 2013 which set out the latest position following the issuing of a technical consultation document in July 2013. The impact on Leeds is a reduction to its Settlement Funding Assessment (SFA – previously referred to as Start Up Funding Assessment) of £81.4m over the next two years.

3 Developing the Council's Financial Strategy - Looking Back - a retrospective view of the Council's financial journey 2010-2013

3.1 The Comprehensive Spending Review 2010 set out the Government's plans to eliminate the structural deficit by the end of the current parliament. This presented a significant financial challenge to the Council which was without precedent in recent times. In addition to the reductions in Government funding the Council has also faced significant costs particularly within adult and children's social care and reductions in income due to the economic climate. The following summarises how the Council's financial plans have changed between 2010 and 2013 to deal with these issues:

- Funding from government has reduced by £94.4m from its 2010/11 levels
- We are spending £10m more on looked after children in 2013/14 compared to the 2010/11 budget, although numbers are down from their peak in 2011/12
- Demographic changes plus the transfer of functions from health (£9.8m) mean we are spending £16m more on people with learning disabilities
- Adult social care services are also spending £4.4m more with external providers, reflecting a move from in-house to independent sector delivery, although this is more than offset by a reduction in staffing costs within the service
- The cost of landfill tax and disposal costs have increased by £2.7m

To deal with these changes

- We are spending almost £50m less on employees, as 2,250 full time equivalent staff have left or are budgeted to leave by 31.3.14
- We have generated around £15m more income from fees and charges and other income sources
- Despite a three year council tax freeze, we have increased income from council tax by £14.2m
- We are generating £4.3m growth from business rates in 2013/14
- Spend on highway maintenance has reduced by £1.8m, partly due to better procurement

- We have reduced our accommodation and overall our annual spend on property has come down by £6.2m; partly offsetting this is additional business rates of £1.8m arising from revaluations
- Through better procurement and demand management we are spending around £25m less on supplies and services
- The Council's efforts to reduce the cost of transport has resulted in a £4.4m saving
- Supporting People spend has reduced by £8.6m reflecting efficiencies and remodelling of the service
- The cost of funding the Council's capital programme has increased by £10m, but low interest rates and the use of capital receipts to fund PFI rentals has meant a net reduction of £0.7m overall

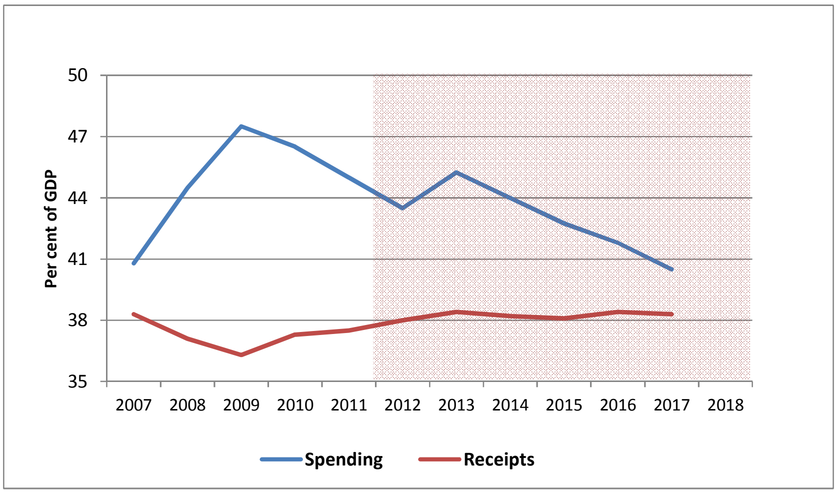
4 National Position

4.1 The Chancellor of the Exchequer announced the 2013 Spending Review on 26th June 2013. The Spending Review sets out the Government's spending plans for central government departments, the NHS and local government for 2014/15 and 2015/16.

4.2 The Spending Review outlines how the Government will continue to reduce the deficit in the public finances by taking difficult decisions to reduce public spending and prioritising investment in infrastructure to deliver a stronger economy. Chart 1 below tracks the annual deficit position with forecast receipts and spending.

Chart 1

Receipts and Spending



Source: Office for Budget Responsibility

4.3 The Government's plan is to reduce overall spending by £11.5 billion in 2015/16, but within that there are a number of variations as summarised below:

- Funding for schools, the NHS and Overseas Development will continue to be protected;
- Funding reductions for unprotected departmental budgets average 5.6%;
- The reduction in funding for local government for 2015/16 is 10.0% in real-terms;

- The Government stated that *spending* across local government will reduce by 2.3%;
- Councils that choose to freeze their council taxes will receive a grant equivalent to a 1% increase for both 2014-15 and 2015-16;
- Councils that choose to increase their council taxes will be subject to a 2.0% referendum ceiling in both years;
- £3.8 billion of health and social care budgets will be commissioned jointly;
- Spending for major infrastructure projects is to be increased by £3 billion a year from 2015-16;
- The Government proposes to top-slice £400m of New Homes Bonus in 2015/16 which would have been given to local authorities, and instead the funding will be pooled and provided to Local Enterprise Partnerships areas (LEPs) to support strategic housing and other economic growth priorities.

4.4 Whilst the funding reduction for Local Government is 10% in real terms (8.2% cash), within those figures are a number of funding streams which have been top sliced and will be subject to a bidding process and not allocated to all authorities, and therefore government funding for core local government services will reduce by 13.1% in cash terms, or 15% in real terms.

4.5 It is also clear that the reduction in Settlement Funding Assessments will not evenly impact upon local authorities, with the reduction for some authorities being less than 10%. For Leeds the cash reduction for 2015/16 is forecast as 14.7%, compared to the national average of 13.1%.

4.6 In addition, the funding mechanism for NHS Clinical Commissioning Groups is currently under review. The Advisory Commission on Resource Allocation has recommended a new allocation formula that is more heavily weighted towards population with the influence of other factors such as deprivation and morbidity being reduced. The overall effect of these proposals if implemented would be to move CCG resources from northern England and London to the South, the Midlands and Eastern England. West Yorkshire under these proposals could expect to lose around £87 per head or 7.4%. Final decisions on the formula and the pace of change are not expected until December 2013. The new arrangements are expected to be in place for 2015/16.

5. Developing the Council’s Financial Strategy - Looking Forward

5.1 The additional 1% reduction to the indicative settlement for 2014/15 as announced in the Government’s budget 2013 has now been confirmed. The total funding reduction for Leeds is therefore £35.9m in 2014/15. For 2015/16, the reduction is £45.5m, giving a total reduction of £81.4m over the two years as shown in the table below.

Table 1

	2013/14 £m	2014/15 £m	2015/16 £m
Settlement Funding Assessment	**346.449**	**310.544**	**265.048**
Reduction (£m)		-35.905	-45.496
Reduction (%)		-10.4%	-14.7%

5.2 Whilst the government has not announced any indicative figures for 2016/17 the downward trend in public spending is thought likely to continue. However, due to this uncertainty, the proposed Medium Term Financial Strategy (MTFS) only covers 2014/15 and 2015/16, but this will be kept under review as delivery of the plan progresses.

5.3 The MTFS does not attempt to provide a detailed budget for the next two years, but is designed to set out the main financial issues facing the Council and to identify and target areas for the delivery of efficiencies and savings. A summary of the budget gap is shown at Appendix 1, and the key assumptions are as follows:

- By the end of 2015/16 the current forecast is a reduction in Settlement Funding Assessment of £81.4m. In general, the strategy assumes that all reductions in specific grants will be matched by reductions in related spending, although this will be subject to review as announcements are made.

- Changes in the Council Tax base – the MTFS assumes an additional 2,500 properties per annum, either being new or brought back into use. The Council not only benefits from the additional Council Tax raised from these properties, but also through the additional funding provided by the Government in the form of New Homes Bonus which is estimated at an additional £3.7m per annum.

- The Government has provided funding for the on-going effect of previous Council Tax freezes up to 2015/16. This is funding that would have otherwise fallen out of the grant system. Additional funding has been provided for those authorities who choose to freeze their Council Taxes for 2014/15 and 2015/16, equivalent to annual increases of 1%. However, a referendum ceiling of 2.0% will apply in each year to those authorities that choose to increase their Council Taxes. A 1% increase in Council Tax would generate an additional £2.3m per annum, although at this stage no assumptions have been made in respect of Council Tax increases in the MTFS.

- Although the business rates baseline will increase year on year, it is anticipated that growth in business rates will exceed this by £2.1m per annum, net of the levy which will support the city region.

- The proposed transfer of the £400m New Homes Bonus to LEPs in 2015/16 referred to in paragraph 4.3 is estimated as a reduction to the Council of approximately £4.7m.

- A number of unavoidable costs and full year effects have also been identified, which will need to be provided for in the strategy for 2014/15 and 2015/16. These are as follows:

    - Limited provision for inflation has been made, most significantly for a 1% pay award in each year. Apart from contractual increases it has been assumed that most other budget headings will be cash limited. However, it has been assumed that fees and charges will increase by at least 3%.

- Provision of £8.7m over the period has been made for demand and demographic pressures in Adult Social Care and Children's Services.

- Although the assumption has been made that debt costs can be constrained to their current level, this does assume that the level of debt is maintained at its forecast level at the end of the current year, and that there is no significant increase in interest rates over the period.

- In accordance with the report agreed by Executive Board on 24th April 2013, and as part of the Leeds City Region Deal, an additional £0.4m has been provided in 2014/15 and a further £2.4m in 2015/16 for the Council's contribution to the West Yorkshire Transport Fund via the West Yorkshire Integrated Transport Authority. This decision was based on the assumption that increased contributions to the transport fund would not be included in the Council Tax referendum ceiling. However, the latest guidance from Government is that they will be included and therefore this decision may need to be reviewed.

- It is assumed that Children's Services commence repayment in 2015/16 of the £4m borrowed from school reserves in 2013/14.

- The 2013/14 budget is supported by £2.5m of general fund reserves. At this stage, no assumptions have been made in respect of changing this level of support. The estimated level of reserves are as follows:

General Fund Reserves	2013/14 £m
Opening Balance 1.4.13	23.1
Budgeted usage	-2.5
Small Business Rates Relief	3.4
Estimated Reserves 31.3.14	24.0

- Taking account of the above, it is forecast that the Council will need to generate savings of almost £90m by 2015/16 as detailed in Appendix 1.

6.0 Bridging the Gap

6.1 The Board will recall that Budget Plus was the approach adopted during 2012, following the work on the Commission on the Future of Local Government. This was further developed into the Best Council Plan which was approved by full Council in July 2013. At its heart it is designed to maintain an on-going focus on:

- developing a Medium Term Financial Plan to ensure that the Council's financial position is sustainable;
- ensuring a focus on outcomes and ambitions throughout our budget process;
- encouraging innovation;
- improving coherence;

  - driving cultural change through the values; and
  - improving the clarity of our relationships with our partners

6.2 The plan sets out the Council's ambition to become the best Council in the best city in the UK and identifies a number of objectives to help achieve this.

- **Best Council Objective: ensuring high quality public services**. The Council has adopted a refreshed procurement policy centred on a category management and a whole lifecycle approach to procurement with clear accountabilities, structured governance and assurance and incorporating openness and transparency. This will help to deliver additional savings from better procurement to ensure that services are high quality and deliver value for money.

- **Best Council Objective: dealing effectively with the city's waste.** Savings will be generated from the implementation of a long term solution for dealing with waste, further roll out of alternative weekly collections and increasing recycling to help reduce the level of landfill tax. The Council has entered into a contract for the construction and operation of a treatment facility to process residual (non-recycled) household waste over the next 25 years, the majority of which is currently landfilled. This will become fully operational from Spring 2016 and will enable household recycling rates to increase to 55% by 2016 with a longer term target in excess of 60%.

- **Best Council Objective: building a child friendly city**. Through the expansion of Family Group Conferencing and continued investment into other preventative services, it is envisaged that more children will be supported to safely remain within their family and community. If this element of the strategy is a success then, all other things being equal, it is anticipated that an overall reduction in Looked after Children numbers of around 200 is possible over the next 2 years, generating significant savings.

- **Best Council Objective: delivery of the Better Lives programme.** New arrangements that will help local people with care and support needs to enjoy better lives will also generate cost savings over the life of the plan. The Council has already started to introduce new measures that will help local people with care and support needs enjoy better lives than before. The Council has been working with a broad range of organisations to ensure that there are wider care and support choices available and better ways for people to gain access to them. New legislation and recently published national policy proposals have endorsed this direction of travel. The focus will remain on ensuring that people with social care needs can access services earlier and that care and support help reconnect people at risk of isolation back with their communities and delay the need for institutional care.

- **Best Council Objective: promote sustainable and inclusive economic growth.** As detailed in paragraph 5.3, through stimulating sustainable economic growth (including housing growth and regeneration) significant additional income can be generated through the new homes bonus, council tax, business rates and the community infrastructure levy.

- **Best Council Objective: becoming an efficient and enterprising council.** By ensuring the council has an agile and resilient workforce with the right skills and the ability to work flexibly significant savings will be generated. A programme of business improvement and organisational design is underway to achieve this. Further savings will be made through a reduction in city centre office space and a significant reduction in the running costs of the total asset base. Additional income will be generated with the council becoming more entrepreneurial by developing services in new markets.

6.3 The delivery of the Best Council Plan savings is essential to meeting the financial challenge going forward. Each of the objectives can only be delivered by adopting a Team Leeds approach across all services and by the integral involvement of partners. They are undoubtedly challenging and in many instances will carry risks, and will require significant work and prioritisation of resources in order for them to be delivered.

6.4 Assuming full delivery of the Best Council objectives, it is anticipated that sufficient savings will be generated in 2014/15. However, there will be a significant shortfall in 2015/16. It is essential therefore that the Council continues to work closely with its partners to ensure the best use of resources available in the city, including:

- Working with health partners to maximise the city's share of the £3.8bn pooled budget for health and social care services, announced in the June Spending Review.
- Securing a share of the funding streams referred to in paragraph 4.4.
- Working with the Local Enterprise Partnership to deliver the economic regeneration agenda.

6.5 Nevertheless, it is clear that further savings proposals will need to be identified to bridge the remaining gap in 2015/16 and it is inevitable that there will be some impact on front line services.

7.0 Housing Revenue Account

7.1 The Council Housing Investment Strategy has over recent years focused on maintaining Council Housing stock to the Decent Homes Standard and delivering other essential investment in building components, in order to maintain stock at 95% decency. However

- It is becoming an increasing priority to deliver investment in other areas in order to support other city priorities, such as support for older people's housing, and ensure the future sustainability of housing stock.
- It is a strategic priority to tackle fuel poverty and increase the energy efficiency of non-traditional housing stock through the installation of external wall insulation and the replacement of inefficient electrical heating systems.
- An emerging investment priority is the structural and energy efficiency investment need of Leeds' 115 Multi Storey Flats, which will place significant financial pressure on the HRA in the long term.

7.2 The Investment Strategy is increasingly focusing on ensuring the long term sustainability of stock, and so where existing schemes are unsustainable e.g. sheltered bedsits, it is an investment priority to remodel or decommission such schemes.

7.3 There are currently insufficient resources within the HRA to deliver in full against all of the above investment priorities, and so it will increasingly be necessary to prioritise some investment across all of the investment areas. The Council is currently undertaking structural surveys of its Multi Storey Flats, and from this will be in a position to review the long term investment need of stock and determine to what extent investment can be delivered against these priorities.

7.4 Progress against these priorities is demonstrated by July's Executive Board agreeing to a £42m investment in new Council housing which will increase the Housing Stock by approximately 400 properties including extra care housing. Since the implementation of HRA self-financing, which replaced housing subsidy, resources available to support capital have increased by 59% or £21.6m when compared to April 2011.

7.5 Underpinning the Housing Revenue Account, and therefore the delivery of housing priorities, is the achievement of the rental income streams that are detailed in the Council's Housing Revenue Account Business Plan. The adoption of a rent model which smoothed out the rent increases assumed in the Government's debt settlement with the Council, meant that significant increases assumed by the Government in rent in the early years of the self- financing settlement could be managed, but without ultimately disadvantaging investment so that the Council can continue to deliver on its housing priorities.

7.6 In July 2013 CLG wrote to stock holding authorities confirming their intention not to extend rent convergence beyond 2014/15. (Rent restructuring was introduced by Government in 2002 with the aim that local authority and housing association tenants would eventually pay similar rents for similar properties in similar areas (rent convergence)).

7.7 This means that for those elements of the housing stock that have not reached convergence by this date, estimated to be 64%, rent increases of CPI+1% would apply instead of the rent increases assumed in the approved HRA Business Plan. The impact of this is to reduce future rental income streams by £6.5m or 3% per annum from 2016/17. In order to address this shortfall, and the consequential impact upon the resources available for capital investment, the Council will revisit its current rent strategy.

8.0 Next Steps

8.1 The Council has been successful in responding to the challenging reductions to its funding since 2010. The Council has identified significant savings over the period through smarter procurement, generating additional income, staffing savings and improvements in efficiency. However, the Council faces significant further reductions in funding over the next two years which will present at least as great a challenge as the savings achieved to date, with an expectation that reductions in Government grant will continue into the next spending review.

8.2 The proposed Medium Term Financial Strategy can only be seen as an interim solution in that it provides a high level framework to help the Council in responding to this challenge and it will underpin the detailed budget setting process for 2014/15. Further work is needed to develop the Council's strategy for 2015/16 and indeed beyond, and a further update for 2015/16 will be provided as part of the 2014/15 budget.

8.3 The Initial Budget Proposals for 2014/15 will be presented to Executive Board in December 2013, which will be subject to further public consultation.

9.0 Corporate Considerations

9.1 Consultation and Engagement

9.1.1 Following on from a successful "YouChoose" consultation on the budget priorities of the Council carried out in 2012, feedback to communities how these priorities have been addressed in the 2013/14 budget has been published and a further survey as to whether these priorities are still relevant going forward is currently being undertaken. This will be followed up by further consultation on the initial budget proposals for 2014/15 which will be presented to Executive Board at their December 2013 meeting.

9.2 Equality and Diversity / Cohesion and Integration

9.2.1 This report does not have any specific implications for equality and diversity nor for cohesion and integration, but it should be noted that the Council's budget process is subject to equality impact assessments as appropriate.

9.3 Council Policies and City Priorities

9.3.1 This report does not in itself have direct implications for Council policies and City Priorities, but it is recognised that the MTFS has been developed within the context of ensuring that resources are aligned to the Council's Best Council ambitions.

9.4 Resources and Value for Money

9.4.1This is a revenue financial report and as such all financial implications are detailed in the main body of the report.

9.5 Legal Implications, Access to Information and Call In

9.5.1 There are no legal implications arising from this report.

9.6 Risk Management

9.6.1 The Council's current and future financial position is subject to a number of risk management processes. Failure to address medium-term financial pressures in a sustainable way is identified as one of the Council's corporate risks, as is the Council's financial position going into significant deficit in the current year resulting in reserves (actual or projected) being less than the minimum specified by the Council's risk-based reserves policy. Both these risks are subject to regular review. In addition a financial risk register is maintained that details the risk and consequences, existing controls to mitigate against the risk, the value in monetary terms of the risk, review dates and progress towards managing the risk within existing resources. The register is prepared before the start of each financial year and is monitored and reviewed on a regular basis.

9.6.2 It is recognised that the proposed strategy carries a number of significant risks. Delivery of the savings and efficiencies proposed will be difficult, but failure to do so will inevitably require the Council to start to consider even more difficult decisions which will have far greater impact upon the provision of front line services to the people of Leeds.

10. Recommendation

10.1 Members are asked to approve the Medium Term Financial Strategy 2014/15 to 2015/16, and to note that this will form the basis for the detailed preparation of the Initial Budget Proposals for 2014/15.

11. Background documents[1]

None

[1] The background documents listed in this section are available to download from the Council's website, unless they contain confidential or exempt information. The list of background documents does not include published works.

Medium Term Financial Strategy 2014/15 – 2015/16

Appendix 1

	2014/15 £m	2015/16 £m	Reduction from Base £m
Funding			
Government Funding			
Settlement Funding Assessment	35.9	45.5	81.4
Small Business Rate Relief	-3.4	0.0	-3.4
New Homes Bonus	-3.7	-3.7	-7.4
NHB - transfer to LEPs	0.0	4.7	4.7
Sub-total Government Funding	28.8	46.5	75.3
Locally Determined Funding [1]			
Assumed growth in Council Tax Base	-2.9	-2.9	-5.8
NNDR Growth	-2.1	-2.1	-4.2
Sub-total Locally Determined Funding	-5.0	-5.0	-10.0
Total Funding Reduction	**23.8**	**41.5**	**65.3**
Unavoidable Costs			
Inflation	8.3	7.3	15.6
Full Year Effects	-3.6	0.0	-3.6
Demand/Demography	4.3	4.4	8.7
School Balances - payback of reserve	0.0	1.0	1.0
Debt	0.0	0.0	0.0
Transport levy [2]	0.4	2.4	2.8
	9.4	**15.1**	**24.5**
Budget Gap	**33.2**	**56.6**	**89.8**

Notes:

1. No assumptions have been made regarding Council Tax increases at this stage
2. This represents the Council's contribution to the West Yorkshire Transport Fund via the West Yorkshire Integrated Transport Authority, as agreed as part of the Leeds City Region Deal