Leeds CITY COUNCIL

Report author: Alan Gay/Doug Meeson

Tel: 74250

Report of the Deputy Chief Executive

Report to Executive Board

Date: 21st October 2015

Subject: Medium Term Financial Strategy 2016/17 – 2019/20

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 support the Council's 'Best Council' and wider 'Best City' aspirations in the context of the Government's spending plans. At its September 2015 meeting, Executive Board agreed a renewed 'Best City' ambition aimed at tackling inequalities: for Leeds to have a Strong Economy and to be a Compassionate City, the Council contributing to this by being a more Efficient & Enterprising organisation. The financial strategy is part of the framework that will help to achieve this ambition.

2. Whilst the precise scale of future reductions in government funding beyond 2015/16 will not be known until the Spending Review and Local Government Settlement are announced in November and December 2015, it is clear from the Chancellor's summer budget and other announcements that the Government's deficit reduction plans will extend through to at least 2019/20, with the announced reductions in public expenditure meaning that further savings will be required.

3. The current and future financial climate represents a significant risk to the Council's priorities and ambitions, and whilst we have been able to successfully respond to the challenge so far, it is clear that the situation will be increasingly difficult over the coming years. Although the Council has a basic legal duty to set a balanced budget, there are clearly also strong organisational reasons for ensuring that we have in place sound arrangements for financial planning and management. The financial strategy and annual budget, as well as a means of controlling spending to

the available resources, is also a financial expression of the Council's ambitions, policies and priorities. Whilst the annual budget setting process can simply be seen as a year by year exercise, it is clear that this needs to be set within a context of a medium-term financial strategy. This is all the more critical given the financial challenges that we are facing.

4. The Council has a comprehensive approach to the development of its financial strategy, its annual budget and the identification of saving plans. Whilst there is currently an unprecedented level of uncertainty around future levels of funding, the Council has a proven history and capability in this area and prudent planning assumptions have been built into the 2016/17 to 2019/20 financial strategy with work underway to develop a range of options to meet the financial challenge.

5. However, there is no doubt that the Council will need to manage the significant challenge of identifying further financial savings and this will prove increasingly difficult over the coming years. While 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 £180m over the past 5 years, we now need to work differently to address this challenge.

6. As set out in the Leeds-led *Commission on the Future of Local Government (2012),* the future of the Council lies in moving away from a heavily paternalistic role in which we largely provide services, towards a greater civic leadership role: working with people, not doing things to or for them. This shift has considerable implications for the way in which the Council makes decisions, develops strategies and its financial and workforce planning. It requires a sound understanding of people's needs and their demands (now and in the future) and a greater level of engagement with the citizens of Leeds.

7. On the 5th October 2015, the Chancellor set out major plans to devolve new powers from Whitehall to local areas to promote growth and prosperity. By the end of the current Parliament, local government will be able to retain 100% of local taxes – including all of the £26 billion of revenue from business rates. Although these changes will have a significant impact on the Council's core funding mix, there is as yet insufficient detail behind the headline announcement to make any informed changes to the figures at appendix 1.

8. The financial strategy does not attempt to provide a detailed budget for coming 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 of £146m. The Initial Budget Proposals for 2016/17 will be brought to the Executive Board on the 16th December 2015.

Recommendation

9. Members are asked to approve the Medium Term Financial Strategy 2016/17 – 2019/20 and agree that the assumptions and principles outlined in this report will be used as a basis for the detailed preparation of the 2016/17 Initial Budget Proposals and will inform the Council's future priorities and strategies.

1. Purpose of report

1.1 This report sets out for the Executive Board the principles and assumptions underlying the proposed financial strategy covering the years 2016/17 to 2019/20. This will provide the framework for the preparation of the 2016/17 Initial Budget Proposals which will be presented to Members in December 2015 and will inform the council's future priorities and strategies.

2. Background information

2.1 The last report on the Medium term Financial Strategy was considered by Executive Board in October 2014. The financial strategy has now been updated to reflect the 2015/16 budget, the latest announcements in respect of government funding and updated cost pressures.

2.2 Whilst the precise scale of future reductions in government funding beyond 2015/16 will not be known until the Spending Review and Local Government Settlement are announced in November and December 2015, it is clear from the Chancellor's summer budget and other announcements that the government's deficit reduction plans will extend through to at least 2019/20, with the announced reductions in public expenditure meaning that further savings will be required.

2.3 The current and future financial climate represents a significant risk to the Council's priorities and ambitions, and whilst we have been able to successfully respond to the challenge so far it is clear that situation will be increasingly difficult over the coming years. Although the Council has a basic legal duty to set a balanced budget, there are clearly also strong organisational reasons for ensuring that we have in place sound arrangements for financial planning and management. The financial strategy and annual budget, as well as a means of controlling spending to the available resources, is also a financial expression of the Council's ambitions, policies and priorities. Although the annual budget setting process can simply be seen as a year by year exercise, it is clear that this needs to be set within a context of a medium-term financial strategy. This is all the more critical given the financial challenges that we are facing.

2.4 On the 8th July 2015, the Chancellor presented a budget that set out Government's plans to tackle the deficit and a broad range of policy changes around welfare, housing, tax, a new Living Wage and devolution. It also signposted a Comprehensive Spending Review for local government and the public services. More detail came on 21st July when the Treasury launched, '*The Spending Review: "A country that lives within its means".*' This document confirmed government's intention to continue the deficit reduction programme with a further £20bn of "consolidation" by 2019/20, in addition to the £17bn announced shortly before in the summer budget. Treasury also asked government departments to set out plans for reductions to their resource budgets based on two scenarios: 25% and 40% savings in real terms by 2019/20. With Schools, the NHS, Defence and International Development continuing to be protected, the public sector contribution to tackling the deficit will fall more heavily on 'unprotected' departments, including Communities & Local Government.

2.5 In the light of further anticipated Government spending reductions through to at least 2019/20, it is important that the Council has a robust financial strategy in place to support the delivery of its ambitions and priorities over the next four financial years.

2.6 The financial strategy does not attempt to provide a detailed budget for the coming 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 of £146m. Initial Budget Proposals for 2016/17 will be brought to the Executive Board on the 16th December 2015.

2.7 The financial strategy recognises and supports the ambition to be the 'Best City in the UK' and the Council's ambition to be the 'Best Council in the UK'. The financial strategy is part of the framework to help achieve the best city outcomes all aimed at tackling inequalities: for Leeds to have a Strong Economy and to be a Compassionate City and for the Council to be a more Efficient & Enterprising organisation. Members are also referred to the 'Strong Economy, Compassionate City' report on today's agenda which details some of the key themes and practical steps we can take to make a difference in these areas, in response to the White Paper motion passed at July's Council on sharing economic success in the city.

3. The Council's Financial Strategy – Looking Back

3.1 Since 2010, councils have dealt with a 40% real terms reduction to their core government grant. In adult social care alone, funding reductions and demographic pressures have meant dealing with a £5 billion funding gap. Even in this challenging context, local government has continued to deliver. Public polling nationally has shown that roughly 80% of those surveyed are satisfied with local services and that more than 70% of respondents trust councils more than central government to make decisions about services provided in the local area – a trend that has been sustained during the last five years.

3.2 Between the 2010/11 and 2015/16 budgets, the Council's core funding from Government will have reduced by around £180m and in addition the Council has faced significant demand-led cost pressures. This means that the Council will have to deliver reductions in expenditure and increases in income totalling some £330m by March 2016. To date, the Council has responded successfully to the challenge and has marginally underspent in every year since 2010.

3.3 The Council's response to these challenges has been to seize the opportunity to shape our own future. Building on the idea of civic enterprise, born out of the Commission for Local Government which was conceived and led by the Council, the approach to and taking control of our own destiny is captured in our vision for Leeds to be the best city in the UK. We have three key themes which drive our work to become the best city: for Leeds to have a strong economy and to be a compassionate city and for the council to become more efficient and enterprising. Through our restorative practice approach, our aim is that communities will be less reliant on the state and more resilient. Consequently, the Council has focussed on the fundamental causational factors by stimulating good economic growth and creatively managing demand for services. In addition, we have also implemented a significant programme of more traditional efficiencies but firmly believe it is the former activity that will create sustainable solutions.

3.4 **Strong Economy:** Leeds has weathered the recession better than many of its neighbours which is in no small part due to the work of city partners in creating the right conditions for growth. Despite austerity, our ambition remains undiminished. Key economic achievements include:

- Work placed employment is now back to pre-recession levels.
- GVA per worker £43k amongst highest outside London.
- New Homes Bonus - over 11,500 new/refurbished dwellings (band D) projected since 2010/11 generating in excess of £58m over the period.
- Progress on delivery of £104m of major infrastructure projects including the flood alleviation scheme, the Aire Valley and Kirkstall Forge.
- The Council will pay a Real Living Wage of £8.01 per hour for all staff from April 2016 giving a £3m boost each year to the local economy.
- In 2013, the 13,000 capacity First Direct Arena opened generating a £55m boost to the local economy.
- In 2014, Leeds hosted the Tour de France Grand Départ which boosted the Leeds economy by £17m.
- A longer-term economic boost to local economy through the City's declared intention for Leeds to bid for the European City of Culture 2023.
- Leeds will host the World Triathlon Series with an anticipated boost to the local economy of £3.5m.
- A Council capital programme in excess of £1bn which is focussed on delivering economic regeneration.

These successes have created a strong economy where fewer people rely on the state and communities are more resilient. This has a direct impact on the council's financial position and enables us to meet many of our compassionate city ambitions: for example housing and business growth has brought funding directly into the council.

3.5 **Compassionate City:** from both a city and council perspective there have been a number of successes in terms of our ambition to be a compassionate city, including:

- The numbers of children who are looked after by the local authority continue to safely reduce.
- Infant mortality rates are at an all-time low.
- Public health programmes and NHS health checks have led to a decrease in smoking rates, helping to reduce deaths from cardio-vascular disease.
- The Council's Better Lives programme is increasing the number of people able to live independently in their own homes.
- Over 14,000 local residents have been supported to improve their skills.

3.6 **Enterprising and efficiency:** The Council's approach to managing funding reductions has been successful to date to the extent that challenging savings and reductions have been delivered whilst continuing to prioritise services that support the most vulnerable across the city. These include;

- Staff reductions of over 2,500 ftes by March 2016, saving £55m per year on employee costs.
- Savings of over £35m through better procurement

- Asset review programme – getting the most from the assets we own and investing in new assets where it makes financial sense. Saving over £4m since 2013/14.

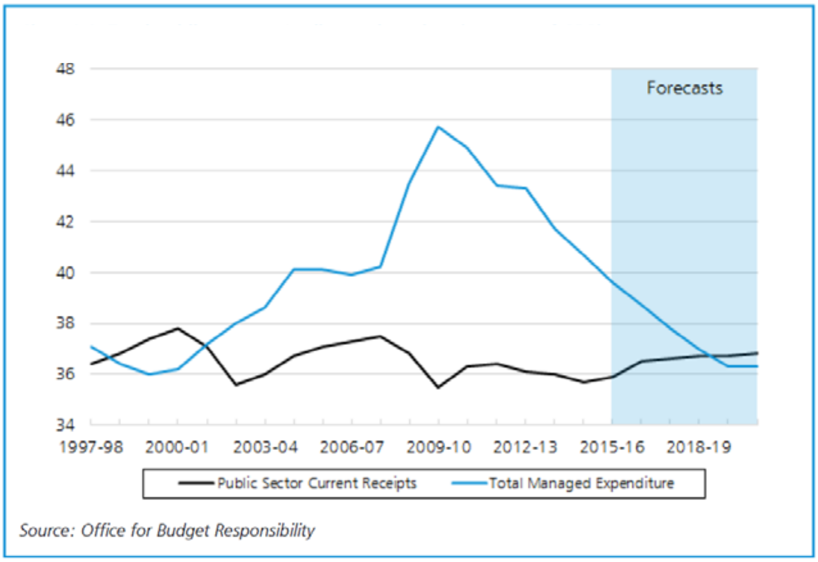
3.7 It is notable that the proportion of the Council's total spend on Children's Services and Adult Social Care has increased from 48.5% in 2010/11 to almost 60% in 2015/16.

3.8 It is significant that despite the funding reductions and spending pressures, through effective strategic financial planning, annual budget setting and robust budget monitoring, the Council has consistently managed to achieve an underspend in each financial years from 2010/11 through to 2014/15. This has enabled the Council to use its general fund reserves each year in a planned way to help manage with the timescales associated with funding reductions and service change/transformation.

4. Local Government Funding – the National Context

4.1 In the summer budget announced on the 8th July 2015, the Chancellor set out the Government's fiscal plan and re-affirmed the Government's commitment to deliver an overall surplus and reduce debt year on year.

Graph 1 Total public sector spending and receipts (per cent of GDP)



Source: Office for Budget Responsibility

4.2 The budget articulated £12 billion of savings from welfare with a commitment to a higher wage, lower welfare, lower tax national economy that is more productive. In addition, Government identified £5 billion from addressing avoidance, evasion and imbalances in the tax system. The key headlines within the budget were:

- The deficit will be cut at the same pace as in the last Parliament which is marginally slower than previously anticipated.
- Planned spending reductions amount to £37 billion over the course of the Parliament with £12 billion of reductions in welfare, £5 billion from taxation

and the remaining £20 billion which will be delivered through the Spending Review.

- The Office for Budget Responsibility's (OBR) Departmental Expenditure Limits (DELs) totals increased substantially compared to the March 2015 budget and in particular in 2016/17 with an increase of £4 billion signalling that the planned spending reductions will be managed over a longer time-period than previously anticipated.
- Public Sector pay rises will be capped at 1% a year for four years from 2016/17.

Table 1 Spending reduction plans over this Parliament (£ billion)

	2016-17	2017-18	2018-19	2019-20
Discretionary consolidation	**9**	**20**	**31**	**37**
Of which announced at Summer Budget 2015	**6**	**9**	**13**	**17**
Of which welfare reform	5	7	9	12
Of which tax avoidance and tax planning, evasion and compliance, and imbalances in the tax system	1	2	4	5
Remaining consolidation	**3**	**11**	**18**	**20**

Source: Office for Budget Responsibility, HM Treasury policy costings and HM Treasury calculations

4.3 The summer budget 2015 confirmed the Government's commitment to fund increases in the NHS and defence spending. The government also remains committed to meeting its target of spending 0.7% of GNI on Official Development Assistance (ODA), and is protecting schools funding on a per-pupil basis including pupil premium rates. Alongside protecting these specific areas, the Spending Review will prioritise spending according to a number of core outcomes:

- Promoting innovation and greater collaboration in public services
- Promoting growth and productivity, including through radical devolution of powers to local areas in England
- Delivering high-quality public services, such as the NHS
- Promoting choice and competition
- Driving efficiency and value for money across the public sector

4.4 Subsequently, on the 21st July 2015 Treasury launched the Spending Review: 'A country that lives within its means' which asked government departments to draw-up plans to help to deliver the further £20 billion of spending reductions overall, over the next 4 years (2016/17 through to 2019/20).

4.4 Government will formally set out the Spending Review on the 25th November 2015, with a subsequent finance settlement for local government likely in mid-December 2015.

5. Developing the Council's Financial Strategy – Looking Forward 2016/17-2019/20

5.1 The medium term financial strategy does not attempt to provide a detailed budget for the coming 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.

5.2 The strategy is built upon a series of key assumptions and estimates primarily around the levels of funding from Government, business rates, council tax and also assumptions around rising costs, for example the rising costs of employment, demographic pressures, etc.

5.3 Funding Envelope

5.3.1 Settlement Funding Assessment

5.3.1.1 Each year the Government announces a Local Government Finance Settlement in which it sets out the total funding available for local government, including Business Rates income and the amount it intends to make available to each individual council. The total amounts allocated to each council are termed "Settlement Funding Assessments" (SFAs). Around 46% of the 2015/16 SFA will be paid directly to local authorities as Revenue Support Grant (RSG). The remaining 54% - known as baseline funding - will come from Business Rates. The starting point for the calculation of SFA is the Business Rates baseline with Revenue Support Grant as a 'balancing item' between the business rates baseline figure and the total SFA, and therefore it is the level of RSG that is reduced to reflect a reduction in SFA.

5.3.1.2 Whilst there is currently an unprecedented level of uncertainty around future levels of government funding, the forecasts included in the financial strategy are based on OBR Fiscal Outlook data to model the potential impact of the changes to Government Departmental Expenditure Limits on the Council's budget. The modelling assumes that funding for schools, the NHS, defence and International Development are maintained in real terms, and that funding reductions would fall equally on the other government departments, including local government. Over the 4-year period, by March 2020 the total reduction in the Council's settlement funding assessment is forecast to be £69.5m or 25.9%.

Table 2- Forecast Settlement Funding Assessment

	2015/16 £m	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m	Total Reduction £m
Settlement Funding Assessment	268.1	255.1	232.1	211.6	198.6	
Reduction (£m)		13.0	23.0	20.5	13.0	69.5
Reduction (%)		4.80%	9.00%	8.80%	6.10%	25.9%

5.3.1.3 The anticipated funding reductions for 2016/17 to 2019/20 need to be treated with some degree of caution, as the impact of national reductions upon the Council will not only be affected by any variations in the reductions between government departments, but also the timescales for the reductions and potentially the distribution of resources between local authorities through the Settlement Funding Assessment mechanism.

Based on the assumption that the Business Rates Baseline figure will increase by 2% each year, the implied reduction in the Council's Revenue Support Grant would be £81.3m, or 65% by March 2020.

Table 3 – Forecast Revenue Support Grant and Business Rates Baseline

	2015/16 £m	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m
Revenue Support Grant	124.3	108.4	82.5	59.0	43.0
Business Rates Baseline	143.8	146.7	149.6	152.6	155.7
Settlement Funding Assessment	**268.1**	**255.1**	**232.1**	**211.6**	**198.6**

5.3.2 Business Rates Retention Scheme

5.3.2.1 Leeds has the most diverse economy of the all the UK's main employment centres and has seen the fastest rate of private sector jobs growth of any UK city in recent years. Yet this apparent growth in the economy is not being translated into business rates growth; in fact the Council's business rates income has declined month by month since the start of the 2015/16 financial year and other authorities are reporting similar problems.

5.3.2.2 Under the Business Rates Retention (BRR) scheme which was introduced in 2013/14, business rates income is shared equally between local and central government. Local authorities that experience growth in business rates are able to retain 50% of that growth locally. The downside is that local authorities also bear 50% of the risk if their business rates fall or fail to keep pace with inflation, although a safety-net mechanism is in place to limit losses from year to year to 7.5% of their business rates baseline. Although BRR allows local authorities to benefit from business rates growth, it also exposes them to risk from reductions in rateable values. The system allows ratepayers and their agents to appeal against their rateable values if they think they have been wrongly assessed or that local circumstances have changed. When agreement cannot be reached, appeals may be pursued through the Valuation Tribunal and then through the courts. One major issue with the system is that successful appeals are usually backdated to the start of the current Valuation List, i.e. 1st April 2010, and this greatly increases the losses in cash terms – by nearly six times in the current financial year. At end of September 2015 there were approximately 6,500 appeals outstanding in Leeds and the total rateable value of the assessments with at least one appeal outstanding totals some £485m, which equates to more than half of the total rateable value of the city.

5.3.2.3 As part of the normal process for reviewing the 2014/15 accounts, under proper accounting practice, the Council identified a post balance sheet adjustment to the collection fund account and specifically to increase the level of provision for business rate appeals by some £23.9m to £41.5m. This adjustment reflected the latest information from the Valuation Office. The worsening position was due to a combination of factors which included an increase in the number of appeals, an increase in the success rate of those appeals that were being resolved and also a significant number of downward revisions to valuations by the Valuation Office on their own initiative. As a result of the worsening position on business rates in 2014/15, the council was no longer required to make a levy payment in that financial year.

5.3.2.4 The financial strategy includes an allowance of £11.9m in 2016/17 which recognises the worsening position on business rates and the contribution required from the general fund to the collection fund. This £11.9m is in addition to the £6.4m contribution in 2015/16 which will also carry-forward into 2016/17. The overall contribution in the financial strategy from the general fund in 2016/17 is therefore £18.3m. This contribution assumes a certain level of business rates growth which recognises the continuing improvement of the economic climate across the city.

5.3.2.5 On the 5th October 2015, the Chancellor set out major plans to devolve new powers from Whitehall to local areas to promote growth and prosperity. By the end of the current Parliament, local government will be able to retain 100% of local taxes – including all of the £26 billion of revenue from business rates. It is worth noting that whilst local government as a whole will retain 100% of the business rates, some degree of re-distribution across the country will still be necessary within the system to take account of the significant differences between rate yields and needs in some areas. Government has also signalled an intention to abolish the Uniform Business Rate and give local authorities the power to cut business rates to boost enterprise and economic activity in their areas. Local areas which successfully promote growth and attract businesses will therefore keep all of the benefit from increased business rate revenues. At the same time, the core Revenue Support Grant will be phased out, and local government will take on new responsibilities.

5.3.2.6 The Chancellor has also announced that under devolution arrangements an Elected Mayor will be given the power to levy a supplementary rate, described as an “Infrastructure Levy”; this will be subject to the support of local businesses and would be limited by a cap which is likely to be set at 2p on the rate.

5.3.2.7 Although these changes will have a significant impact on the Council’s core funding mix, it is not expected that they will have any impact on the 2016/17 settlement.

5.3.3 **Council Tax**

5.3.3.1 The 2015/16 budget was supported by a 1.99% increase in the level of Council Tax which remains the 2nd lowest of the Core Cities and mid-point of the West Yorkshire districts.

Table 4 – 2015/16 Council Tax levels

Core Cities	Band D	West Yorkshire Districts	Band D
	£		£
Nottingham	1,459.67	Kirklees	1,267.15
Bristol	1,419.01	Calderdale	1,251.43
Liverpool	1,384.53	Leeds	**1,168.80**
Newcastle	1,380.82	Wakefield	1,161.43
Sheffield	1,308.28	Bradford	1,152.11
Manchester	1,172.27		
Leeds	**1,168.80**		
Birmingham	1,158.43		

(Figures exclude Police and Fire precepts)

5.3.3.2 Government previously provided funding for the on-going effect of previous Council Tax freezes up to 2015/16. The Council accepted the Council Tax freeze grant for the years 2011/12 to 2013/14, and government funding of £9.428m was built into the Council's 2015/16 settlement (the grant for freezing Council Tax in 2012/13 was for one year only). The financial strategy continues to assume that this funding will continue into 2016/17, but currently there is no certainty as to this.

5.3.3.3 At this stage, the financial strategy makes no assumption about an increase in Council Tax in future years. For information, a 1% increase would generate additional income of approximately £2.5m in 2016/17. Whilst Government has yet to confirm any detail regarding Council tax capping, any increase in Council Tax in future years is likely be subject to the Government's referendum limit, which for 2015/16 was set at 2%.

5.3.4 **Specific Grants - Public Health Grant**

5.3.4.1 The allocation of the main ring-fenced Public Health grant funding for 2015/16 was frozen at 2014/15 levels at £40.5m. In addition, the responsibility for the 0-5 years services which include health visiting services and Family Nurse Partnership will transfer to the Council from October 2015 with further funding of £5m.

5.3.4.2 However, on the 4th June 2015, Government announced a national £200m in-year reduction in the 2015/16 for the Public Health grant. At the end of July Government issued a 4-week consultation with a closing date of 28th August with a preferred option, based on ease of implementation, of a flat-rate cut across all local authorities, regardless of local needs and circumstances, for Leeds, this would amount to a funding cut of £2.8m. This would equate to a 7% cut of the current public health budget prior to the planned transfer in October 2015 of the commissioning responsibilities for health visiting services.

5.3.4.3 Whilst the Public Health grant for 2015/16 is already committed, work has been undertaken to identify potential savings and understand the resulting impact. Managing reductions of this scale at such a late juncture in the financial year will inevitably see reductions in general public health services which are provided through the Council, NHS bodies and the 3rd sector and will impact on services such as health protection, tobacco control, healthy lifestyles, drug & alcohol services, health-checks and specific targeted support for vulnerable children and adults. Executive Board approved the changes to the budget to reflect the potential reduction to the public health grant and proposed savings, subject to confirmation of the final in-year grant.

5.3.4.4 At this stage there is no firm information that this cut will be recurrent although it is anticipated that this will be confirmed through the Spending Review. In line with the general principle applied to reductions in specific grant funding, the financial strategy assumes that any reduction in the public health grant will be matched by a corresponding reduction in related spend.

5.3.4.5 **Other specific grants** – as a general principle, the strategy assumes that variations in specific grants will be matched by reductions in related spending, for example non-recurrent grant funding such as the DfE Innovation Fund, and other potential grant reductions such as the Youth Offending grant, the Education Support grant and the Housing Benefit Administration grant, although this will be subject to review as announcements are made and implications fully understood.

6. Changes in Costs

6.1 **Inflation** - the financial strategy makes allowance for £33.6m of net inflation across 2016/17 through to 2019/20. This includes provision of £4m each year for a 1% pay award in each year over and above the cost of implementing the living wage. The financial strategy makes allowance for inflation where there is a contractual commitment, but anticipates that the majority of other spending budgets are cash-limited. An anticipated 3% rise in fees and charges has also been built into the financial strategy.

6.2 **Employer's National Insurance** - employer's national insurance costs are due to increase in 2016/17 as announced in the Chancellor's Autumn Statement in 2013. The cost of this in 2016/17 would amount to £7.7m of which £7m relates to general fund services and £0.7m to the Housing Revenue Account. The Chancellor had previously indicated that public sector funding would take this additional burden into account, although given the overall position on government funding the Council has taken a realistic view and made provision in the financial strategy.

6.3 **Real Living Wage** – at its September 2015 meeting, the Executive Board noted that Council staff would be paid a real Living Wage at £8.01 per hour from the 1st April 2016 with the decision to be implemented by the Deputy Chief Executive. The latest estimated cost of implementation to the general fund is £2.6m in 2016/17 with additional costs of £0.7m in 2017/18 and 2018/19 and a further increase of £1m in 2019/20. In addition, the cost to the Housing Revenue Account would be in the region of £0.2m in 2016/17 with the impact for schools-based staff being around £2.1m. These calculations are based on the Campaign for Living Wage Foundation hourly rates which at September 2015 were set at £7.85 per hour (outside London), and which are due to be reviewed in November 2015.

By paying a real Living Wage of £8.01 per hour from the 1st April 2016, the Council is not committing to automatic indexed future increases. Any future increases will need to take into account recommendations from the Living Wage

Foundation, any national pay increases, affordability and the financial circumstances of the Council.

6.4 **Demography** – the financial strategy also recognises the increasing demography pressures in Adult Social Care with provision of £22.1m across the life of the strategy. The population growth forecast assumes a steady increase from 2015, in the number of people aged 85 -89 during 2016 and 2017 (2.9% and 2.8% respectively) followed by further increases but at a lower rate at 1.8% for the later years of the strategy, resulting in additional costs for domiciliary care and placements (£3.5m). In addition, the strategy reflects the anticipated impact of increasing cash personal budgets of £2m across through to 2020. The Learning Disability demography is expected to grow by £3.7m per annum, which includes an anticipated growth in numbers of 3.5% (based on ONS data) over the period; but noting that the high cost increase is primarily a combination of increasingly complex (and costly) packages for those entering adult care, as well as the meeting the costs of the increasing need for existing clients who's packages may last a lifetime.

6.5 **Debt** – the financial strategy makes allowance for an increase in debt costs of £2.5m in 2016/17, £2.1m in 2017/18 and £2m in 2018/19 which reflects the on-going capital programme commitments together with anticipated changes in interest rates. The gross total capital programme is over £1bn and seeks to deliver investment in line with the Council's plans and objectives. The level of the capital programme will continue to be reviewed to ensure that it is deliverable and that it continues to be relevant. The forecast debt costs reflect the costs of financing both present and future borrowing in line with assumed borrowing costs. These assumed borrowing costs will be kept under review and adjusted for the latest market estimates.

6.6 **National Living Wage** – as part of the budget in July 2015, Government announced the introduction of a new National Living Wage of £7.20 per hour, rising to £9 per hour by 2020. Implemented from April 2016, the national Living Wage would be paid to all employees aged over 25.

In addition to the additional cost of implementing the Real Living Wage for all directly-employed staff, the financial strategy also makes allowance for implementing the cost of the National Living Wage for commissioned services. The immediate impact in 2016/17 is estimated at an additional cost of £5.2m with an additional cost of £18.4m by 2019/20.

6.7 **West Yorkshire Transport Fund** – the strategy provides for an increase in the contribution to the West Yorkshire Transport Fund from £5.4m in 2014/15 to £11.4m over 10 years, an increase of £0.6m each year. The Leeds share based on population figures is around £0.2m and provision has been built into the financial strategy to reflect this.

7. Reserves and non-recurrent income

7.1 General and useable reserves are a key measure of the financial resilience of the Council allowing the authority to address unexpected financial pressures.

7.2 The Council's balance of general reserves at April 2015 was £22.3m and after taking into account the budgeted use of £1.4m in 2015/16, will leave an anticipated balance at March 2016 of £20.9m. For 2015/16, the minimum general reserve level was set at £17m.

7.3 At this stage, the financial strategy makes no assumption about the use of general reserves. However, given the uncertainty about future government funding, the financial challenges ahead and the inherent risks in future budgets, there is an argument that the level of general reserves should be increased over the course of the strategy in order to increase the Council's financial resilience.

8. The Budget Gap

8.1 After taking into account the impact of the anticipated changes in funding and spend, it is forecast that the Council will need to generate savings in the order of £146m by 2019/20 as summarised in Appendix 1, although this is very much dependent on the range of assumptions highlighted previously in this report, particularly around the level of future core funding from Government.

8.2 The Council has a comprehensive approach to the development of its financial strategy, its annual budget and the identification of saving plans. Over successive financial years the Council has delivered efficiencies and savings through smarter procurement, generating additional income, better business management and innovative demand management. Whilst there is currently an unprecedented level of uncertainty around future levels of government funding the Council has a proven history and capability in this area and prudent planning assumptions have been built into the 2016/17 to 2019/20 financial strategy with work underway to develop a range of options to meet the financial challenge.

8.3 However, there is no doubt that the Council will need to manage the significant challenge of identifying further financial savings and this will prove increasingly difficult over the coming years. While the Council to date has been successful in responding to the challenging reductions to its funding since 2010 - in the region of £180m over the past 5 years - we now need to work differently to address this challenge.

8.4 As set out in the Leeds-led *Commission in the Future of Local Government (2012),* the future of the Council lies in moving away from a heavily paternalistic role in which we largely provide services, towards a greater civic leadership role: working with people, not doing things to or for them. This shift has considerable implications for the way in which the Council makes decisions, develops strategies and its financial and workforce planning. It requires a sound understanding of people's needs and their demands (now and in the future) and a greater level of engagement with the citizens of Leeds. Much will depend on redefining the social contract: the relationship between the State and the citizen where there is a balance between rights and responsibilities; a balance between reducing public sector costs and managing demand, and improving outcomes. If more people are able to do more themselves, the Council and its partners can more effectively concentrate and prioritise service provision.

8.5 Making these step changes will help to tackle the range of inequalities and challenges that continue to exist in Leeds, as highlighted by the Joint Strategic

Needs Assessment (JSNA) work[1] carried out earlier this year. These include, for example:

- 20% of the Leeds population live in deprived areas, centred in the Inner East and Inner South of the city;
- Educational attainment is one of the main determinants of life chances and though good progress has been made, Leeds is below the national average on some key indicators;
- Housing remains a challenge in terms of affordability, quality and meeting demand;
- Health inequalities continue to impact on the most vulnerable, with increased demand on related public services through growing numbers and increased complexity of needs; and
- Across the city and within localities there is – and will continue to be – significant demographic change through an ageing population, increased birth rate, more transient populations and changing ethnicities. Again, these put additional pressures on public services.

8.6 The 2015 Index of Deprivation was released on 30th September by the Department of Communities and Local Government and while a full analysis will be provided to the Executive Board in November, the data shows that Leeds continues to have a number of neighbourhoods in the most deprived 10% nationally[2]. The Council will need to consider carefully how to address the city's inequalities within the context of its available resources.

8.7 Inevitably, addressing an estimated budget gap of £146m by March 2020 will require the Council to take difficult decisions in order to reduce the Council's net spend. These decisions will unavoidably include reducing and ceasing services and also generating additional income through increasing fees and charges for services, potentially based on the ability to pay.

9. Housing Revenue Account

9.1 The Housing Revenue Account (HRA) includes all the expenditure and income incurred in managing the Council's housing stock and, in accordance with Government legislation, operates as a ring fenced account.

9.2 In July 2015 the Chancellor announced that for each of the next 4 years (2016/17 to 2019/20) housing rents will reduce by 1% each year and then revert back to the previous policy of CPI+1% from 2020/21. For Leeds, this equates to a reduction of £20.5m in rental income over this four year period which will then start to be offset by reverting back to annual rent increases of CPI+ 1% in 2020/21. These reductions in rental income will be required to be managed along with having to absorb pay, price and service pressures.

9.3 The HRA Financial Plan was based on the assumption that rents would increase in line with CPI +1% each year for 10 years as per the Government Policy introduced last year – in essence a 3% increase pa (based on the Government CPI target of 2%). The Chancellor's announcement is therefore effectively a 4%

---

[1] The Joint Strategic Needs Assessment (JSNA) is a rolling programme of needs assessments and analysis with a primary focus on Health and Wellbeing. Its purpose is to influence priorities and inform commissioning strategies and plans. The 2015 JSNA for Leeds focused on population, deprivation, housing, mental health, potential years life lost and learning disabilities.

[2] Leeds has 105 Lower Super Output Areas (LSOA) in the most deprived 10% nationally; 22% of all Leeds LSOAs. LSOAs are the geographical building blocks for the Index of Deprivation with an average of 1,500 residents per LSOA. Leeds has 482 LSOAs in total.

pa reduction from the Plan for each of the next 4 years (2016/17 to 2019/20). When compared to the level of resources assumed in the HRA Financial Plan this equates to a loss of £283m of rental income over a 10 year period (2016/17 to 2024/25).

9.4 The rollout of universal credit in Leeds commenced in 2015 and once fully implemented it will require the Council to collect rent directly from around 24k tenants. This will have implications for the level of rental income receivable.

9.5 Despite the reduction in resources the Council remains committed to the Investment Strategy agreed at Executive Board and the projected loss of rental income will need to be managed through a combination of identifying efficiencies, implementing cost reductions in the HRA and reviewing other sources of income. Further details of these proposals will be incorporated into the Initial Budget Proposals report that will be considered at Executive Board in December.

10. Next Steps

10.1 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, there is no doubt that the Council will need to manage the significant challenge of identifying further financial savings and this will prove increasingly difficult over the coming years. Whilst, 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 £180m over the past 5 years, we now need to work differently to address this challenge.

10.2 As set out in the Leeds-led *Commission in the Future of Local Government* (2012), the future of the Council lies in moving away from a heavily paternalistic role in which we largely provide services, towards a greater civic leadership role. This will be achieved through redefining the social contract to identify the respective responsibilities of the State and the citizen and to improve demand management. This shift has considerable implications for the way in which the Council makes decisions, develops strategies and its financial and workforce planning. It requires a sound understanding of people’s needs and their demands (now and in the future) and a greater level of engagement with the citizens of Leeds. The proposed medium term financial strategy provides a high level framework to help the Council in responding to this challenge and it will underpin the detailed budget setting process for 2016/17 and beyond.

10.3 As per the timetable below, the Initial Budget Proposals for 2016/17 will be presented to Executive Board in December 2015, which will be subject to further public consultation.

23rd Sept 2015	Strong Economy & Compassionate City - Ambition & Draft Outcomes	Executive Board
	Development of options for 2016/17 & 2017/18	Executive Members & Directors
21st Oct 2015	Medium Term Financial Strategy 2016/17 to 2019/20	Executive Board
25th Nov 2015	Comprehensive Spending Review announced	
Mid-December	Draft local government finance settlement announced	
16th Dec 2015	2016/17 Initial Budget Proposals	Executive Board
	Scrutiny and Budget Consultation	
10th Feb 2016	Clearance of 2016/17 budget proposals Refreshed Best Council Plan	Executive Board
24th Feb 2016	Approval of Budget 2016/17	Full Council

11. Corporate Considerations

11.1 Consultation and Engagement

11.1.1 The financial strategy has been driven by the Council's ambitions and priorities which have been shaped through past consultations and stakeholder engagement. It is proposed that public perception evidence that services and localities already hold about people's priorities is brought together and a summary of the findings produced to support the Initial Budget Proposals for 2016/17.

11.1.2 This strategy will provide the framework for the Initial Budget Proposals for 2016/17 and a consultation exercise will be undertaken on these budget proposals following Executive Board in December 2015. As in previous years, residents and wider stakeholders will have the opportunity to comment on the initial budget proposals in a variety of ways, for example hard-copy feedback forms in public spaces, online and also through city-wide networks.

11.2 Equality and Diversity / Cohesion and Integration

11.2.1 This report does not have any specific implications for equality and diversity nor for cohesion and integration, but is should be noted that the Council's budget process is subject to equality impact assessments as appropriate. Tackling inequalities is at the heart of the renewed ambition and therefore equality considerations will be a primary focus when the council is developing its priorities and budget proposals for 2016/17.

11.3 Council Policies and Best Council Plan

11.3.1 The draft set of outcomes as reported to Executive Board in September 2015 will be used to develop refreshed priorities for the Council and will inform a revised Best Council Plan for 2016/17. These will be drawn-up in conjunction with the 2016/17 budget proposals and so seek to ensure that the Council's financial resources are directed towards its policies and priorities and, conversely, that these policies and priorities themselves are affordable.

11.4 Resources and Value for Money

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

11.5 Legal Implications, Access to Information and Call In

11.5.1 There are no legal implications arising from this report.

11.6 Risk Management

11.6.1 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, financial management and monitoring continues to be undertaken on a risk-based approach where financial management resources are prioritised to support those areas of the budget that are judged to be at risk, for example the implementation of budget action plans, those budgets which are subject to fluctuating demand, key income budgets, etc. This risk-based approach has been reinforced with specific project management based support and reporting around the achievement of the key budget actions plans.

11.6.2 It is recognised that the proposed strategy carries a number of significant risks. Delivery of the annual budget 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.

12. Recommendation

12.1 Members are asked to approve the Medium Term Financial Strategy 2016/17 – 2019/20 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 2016/17 and will inform the council's future priorities and strategies.

13. 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.

APPENDIX 1

Medium Term Financial Strategy 2016/17 - 2019/20

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m
Funding Envelope				
Changes in national funding:				
Settlement Funding Assessment Reduction	**13.0**	**23.0**	**20.5**	**13.0**
Changes in local funding				
Increase in the Council tax base	(0.6)	(3.2)	(3.2)	(3.4)
Business Rates Retention	11.9	(8.1)	(0.8)	(3.3)
sub-total	**11.3**	**(11.3)**	**(4.0)**	**(6.7)**
Reduction/(increase) in Funding Envelope	**24.3**	**11.7**	**16.5**	**6.3**
Cost Changes (2015/16 repriced budget)				
Inflation	8.4	8.3	8.4	8.5
National Insurance	7.0			
Capitalised Pension costs	(2.3)	(0.8)	(0.7)	(1.1)
Campaign for Living Wage	2.6	0.7	0.7	1.0
National Living Wage - Commissioned Services	5.2	4.4	4.4	4.4
Demography	5.8	5.7	5.9	4.9
Waste Strategy	(4.0)	0.1		
Debt	2.5	2.1	2.0	
Capitalisation of schools capital spend		2.5		
West Yorkshire Transport Fund	0.2	0.2	0.2	0.2
	25.4	**23.2**	**20.9**	**17.9**
Reduction in Funding Envelope and Cost Changes	**49.7**	**34.9**	**37.4**	**24.2**