ARUN DISTRICT COUNCIL

REPORT TO AND DECISION OF CORPORATE POLICY AND SUPPORT COMMITTEE ON 14 OCTOBER 2021

SUBJECT: Financial Prospects 2021/22 to 2025/26

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EXTN: 37568
AREA: Corporate Support

EXECUTIVE SUMMARY:

The Council's Medium-Term Financial Strategy (MTFS) covering the period up to 2025/26 rolls forward and updates the data in the existing approved MTFS. The Strategy amends certain assumptions contained in it to reflect changes in the Council's circumstances and other issues that have a strategic bearing on the Council's financial prospects.

RECOMMENDATIONS:

Committee is recommended to:

1. Agree the core assumptions set out in the Medium-Term Financial Strategy and the current financial position;

2. Note and agree the significant risks to local government finance that have been outlined in the report; and

3. Approve that the Medium-Term Financial Strategy is to be used to set the Budgetary framework in preparing the 2022/23 Budget

1. BACKGROUND:

This report specifically covers the Council's General Fund as the Housing Revenue Account has its own business plan and financial model. The latest financial forecast has been prepared against a continuing backdrop of unprecedented uncertainty over Government funding and the economy which has, inevitably, been compounded by significant issues connected with the continuing COVID-19 crisis.

This report contains the latest version of the MTFS which uses the most recent information available to forecast the Council's income and expenditure over the next 4 years. The situation is even more fluid than last year as the COVID-19 crisis has created greater uncertainty. It was expected that the spending review would be launched in July 2021, with the Chancellor making an announcement before the summer parliamentary recess.

However, this was delayed until September at the earliest, along with an announcement on social care. The social care announcement has now been made and is discussed below. The delayed “formal launch” will provide “details for how much overall government spending will rise by in the next financial year”. The delay probably also makes a November announcement more likely than October.

The Chancellor’s expected launch statement should give a broad outline of the spending totals that are available – but details about the package for local government in 2022-23 will not be known until later in November, or even the provisional settlement in December 2021. It was hoped the spending review will cover the remainder of the parliament, but the tight timescales might now make a one-year settlement more likely, similar to recent years. This gives rise to difficulties in medium term financial planning.

Recent Institute of Financial Studies analysis states that “government support to local government largely met pandemic-related pressures in 2020-21”, and probably in 2021-22 as well. But “problems loom” from 2022-23 onwards and the sector will require support from central government “potentially running into the billions”. Yet, based on current plans, local government can expect real-terms cuts in funding from 2022-23 onwards. This is shown in the MTFS and discussed further below.

The government’s Fair Funding Review and Business Rates Reforms are now expected to be implemented with effect from 2023/24. These coinciding changes are expected to wipe out the considerable business rates growth that has accrued to the Council since the inception of the current scheme in 2013/14. This leaves the whole situation extremely uncertain as BRRS will be the main source of funding for the Council and makes forecasting an inexact science. Inevitably, informed assumptions on this key variable have had to be made and as there has been no adjustment to the scheme in 2021/22, the changes are expected to materialise from 2023/24. Members have previously been advised there will be a huge detrimental effect on the Council if the accumulated growth is distributed evenly across the country.

The financial effects of COVID have been severe for the Council, in common with other local authorities across the country. The first UK lockdown commenced on 23 March 2020. At that stage, the Council anticipated approximately £1.993m of net additional expenditure and an estimated loss in income of approximately £2.52m during 2020/21. There were noticeable reductions in income from licences and property & estates, whilst Planning income remained buoyant. However, a gradual return of most income streams did occur, although not to the levels previously budgeted for. The Government provided a range of support in the form of grants and relief. For the financial year 2020/21, the Council received a number of grants which included £56m support for businesses, £945k Council tax Hardship fund, £2.37m C-19 support grant, £931k service related and £1m Sales, fees and service support grant.

In addition, there were a number of Business Rates grants schemes initiated by the Government to support Business throughout this pandemic. These were administered by the Council

The Council is eligible for 75% Tax Income Guarantee (TIG) for the loss of income on Council Tax (£62k) and Business rates (£689k) as a compensation for the decrease in collection during 2020/21 due to COVID19.

The Collection Fund had a deficit of £26m at 31 March 2021 – this is repaid by the precepting authorities over future financial years. Arun's share of the deficit of £9.3m is shown in the Collection Fund Adjustment Account and is due to be repaid over a period of three years commencing 2021/22 to 2023/24.

However, due to sound financial management and the welcome central government support, the outturn showed a balanced General Fund and a material increase in earmarked reserve balances at 31 March 2021.

In preparing this report, a number of more detailed assumptions have been reviewed and input into the financial model. This uses a wide range of strategically important financial assumptions and variables to obtain an informed view on year end balances, and to quantify the potential of any capital programme resources whilst maintaining a minimum level of General Fund balances of £4million. The assessment of the various assumptions is always considered carefully whilst taking a prudent view.

It must be appreciated that with a financial strategy it consists of a series of assumptions using the best available information to inform a financial forecast. As in last year, this is even more challenging than in previous years due to delayed expected changes in government funding combined with the ongoing effects of the Corona virus pandemic.

It has therefore been necessary to make changes/updates to some of the previous assumptions to address all of the factors which affect the Council. The principal assumptions made are:

- Council Tax increases by £5 per annum which is currently the maximum allowed for similar District Councils;
- There is an inflationary increase in salary costs in 2022/23. Thereafter an increase of 2% per annum is estimated. The effect of the government's recent announcement increasing National Insurance contributions from 2022/23 is included;
- If possible, the model assumes cash limited sums for goods and services (no inflationary rise) for the period, otherwise inflation is provided for;
- The most up to date figure available has been used for the lump sum payable to the pension fund which was reflected in the latest report from the actuary for 2022/23. At that stage, a triennial valuation is due. Until this is confirmed, it is assumed the 2022/23 figure remains constant over the reporting period.
- It is assumed all discretionary fees and charges imposed by the Council increase by at least 2.5% per year.

It is difficult to model enhancements to the capital programme and to calculate the resources that will be available due to the funding uncertainties and slippage caused by the pandemic. There is, inevitably, a requirement to allow for business-critical IT systems and infrastructure as systems fall out of maintenance/support and become life expired. It is clear that the Council will have to take a prudent approach regarding capital/one off schemes.

It has been assumed that the Council continues with the enhanced capital programme, but this will have to be a subject for discussion and review given the financial challenges that the Council is facing. It is essential that expenditure continues to be prioritised for the essential maintenance programme to ensure that operational assets are maintained at the required standard for service delivery.

The forecast also includes the assumption of £500k for one off pump priming projects to help progress Council priorities. As in previous years the Council will underpin its capital programme with the use of capital receipts to protect scarce revenue resources.

The most volatile and significant variable continues to be the Retention of Business Rates, as detailed above, but a further significant funding source is New Homes Bonus (NHB) which is dictated by housing growth within the District. However, latest information regarding NHB is that the Government will wind down the scheme and no income will be received from 2023/24. No information is currently available for a replacement scheme.

The following section outlines a number of risks that are associated with the MTFS and how these may be mitigated.

2. PROPOSAL(S):

Risks

The most serious financial risk that the Council is facing is the potential implications of changes in Local Government funding as outlined in the preceding section. From 2023/24, if the projections are correct, a material recurring deficit appears on the General Fund Budget.

There are a number of risks around the retention of Business Rates which is the major funding source from central government and will likely be the sole source in future. The effect of COVID19 on the economy and on business rates has made fundamental changes to business rates or, even, replacement with a different business tax much more likely. Whilst the best available information has been used, as outlined above, there is also a risk that the level of business rate appeals will be more than has been anticipated and this risk lies with local government. As mitigation against this significant risk and the detrimental funding changes expected, the Council has enhanced the Funding Resilience Reserve. It is pleasing to note that during 2020/21, a contribution of £833k was made to this reserve increasing the balance to £6.66m. This will provide a valuable buffer when central government funding is anticipated to reduce and will act as a hedge against the economic effects of COVID19. However, this reserve should not, solely, be used for supporting the budget as it could also, potentially be used to pump prime transformational projects. It is acknowledged, however, that this is a temporary finite measure and the underlying funding gap will have to be addressed by the Council.

The proposals concerning NHB are a significant concern and the assumption is that this will be ceased after 2022/23 with no replacement available. Again, all that can be done is to monitor the situation closely and retain a reserve, as outlined above, to address the anticipated funding shortfall.

The income from Council Tax is generally relatively certain but the expected recession resulting from COVID19, and the expected increase in unemployment once the furlough scheme is wound down means there could be an adverse effect on the Council's taxbase (i.e. could offset or wipe out any gains from new dwellings). This would happen if the increase in unemployment caused an increased number of people to seek support from the Council Tax Reduction Scheme which reduces the taxbase. This creates greater risks and uncertainty in forecasting. In addition, as a result of courts being closed during the COVID19 outbreak, implementation of Universal Credits and unable to secure debts with DWP it is proving more difficult to collect Housing Benefit overpayments. This is likely to continue until backlogs are reduced.

There are also other expenditure pressures in a number of areas, notably leisure, especially since reopening the leisure centres, and these will be monitored closely and the effect of these reflected in the financial strategy. Regular meetings are taking place with the Leisure services provider. Latest projections received from the provider indicate that a shortfall in contact income is likely in 2021/22. The Provider projects income levels to be restored by April 2022 so no adjustment has been made to the MTFS for this at this stage.

Due to the United Kingdom leaving the EU, the COVID19 pandemic and extensive forest fires throughout North America and Europe, certain commodities and labour are in short supply. This may have an effect on the Council's ability to provide services and deliver its capital programme.

On 8 September 2021, the government announced its intention to increase National Insurance contributions by 1.25% to assist with funding the National Health Service and assist with the social care funding crisis. The increase will be applicable from 1 April 2022 and is on both employee and employer contributions. This represents an increase of £120k per annum in cost to the Council and is built into the projections.

The Council's current Cleansing contract expires on 31 January 2023. A replacement contract will be procured. There is a risk that a new contract may result in a significant increase in cost. Should this be the outcome, Members will be advised at the earliest opportunity. Obviously, efficiencies and savings will be sought in pre-contract preparation and negotiations.

Whilst the extent of funding cuts on Arun remains largely unknown it is vitally important to mitigate, as much as possible, against such significant risks. The most effective mitigation against this is to hold sufficient balances to ensure that the Council has enough time to plan and implement any reductions in expenditure and are not obliged to make rushed or ill informed decisions. It is also important to ensure that a robust approach is taken to any investment decisions and stipulate that all are accompanied by a thorough business plan which clearly outlines all costs and benefits. In addition, all decisions must be prudent, affordable and sustainable and any planned savings are realised.

Indicative Projections

The following table shows the current situation given all of the assumptions and omissions outlined above. These will be, inevitably, be fine-tuned as more information becomes available and have to be read in conjunction with all of the caveats and uncertainties outlined earlier in the report. It should be stressed that the balances figures are purely indicative and show what the situation would be if no remedial action were to be taken. In practice, the Council will need to fully assess the implications of any reductions in external funding and develop a strategy to make the necessary reductions in net expenditure to ensure a prudent level of balances is maintained.

The effects of the above assumptions are summarised in the table below:

	2021/22 £'000	2021/22 Revised £'000	2022/23 £'000	2023/24 £'000	2024/25 £'000	2025/26 £'000
Net Expenditure	25,897	25,897	26,405	27,076	27,739	28,377
Surplus/ (Deficit)	0	0	(1,510)	(4,515)	(3,774)	(3,415)
Funding Resilience Reserve				4,515	2,144	
Balances	7,076	7,076	5,566	5,566	3,936	521

When considering the figures above it is important to consider the issues outlined earlier in the report and, especially the uncertainty regarding central government funding and they can only be regarded as indicative at this stage. The underlying financial position is masked to a certain extent by the ongoing effects of the COVID19 pandemic, the earmarked reserve contributions, from the Funding Resilience Reserve to cover the reduction in external funding, but the effect of that can be seen above. However, given the expected reduction in funding the trend of deficits is not surprising. It is fortunate that the Council's prudent financial management has resulted in sufficient balances in hand which will enable a strategy with a measured approach to be formulated. In addition, the strategy will be refreshed as detail emerges at the earliest opportunity.

The Council are already taking positive steps to address the sizeable deficit outlined above and recruitment to all vacant posts have to be approved by Corporate Management Team (CMT) before they are recruited to and managers are expected to make savings when recruiting. In addition to this, the Chief Executive is leading on a comprehensive savings exercise with the aim of making significant reductions to the Council's base budget. However, given the additional problems caused by COVID19 this has not progressed as expected. Therefore, it is essential that the Council review and develop a strategy to address the savings target indicated in the table above.

The likely deficit for the 2022/23 budget will be dependent upon any additional Government support that may be announced at the time of the settlement and any dampening for future years.

3. OPTIONS:

1. To accept the assumptions outlined in the strategy.

2. To not accept the assumptions outlined in the strategy.

4. CONSULTATION:

Has consultation been undertaken with:	**YES**	**NO**
Relevant Town/Parish Council		✓
Relevant District Ward Councillors		✓
Other groups/persons (please specify)		✓

5. ARE THERE ANY IMPLICATIONS IN RELATION TO THE FOLLOWING COUNCIL POLICIES: (Explain in more detail at 6 below)	**YES**	**NO**
Financial	✓	
Legal	✓	
Human Rights/Equality Impact Assessment		✓
Community Safety including Section 17 of Crime & Disorder Act		✓
Sustainability	✓	
Asset Management/Property/Land	✓	
Technology		✓
Other (please explain)		✓

6. IMPLICATIONS:

To formulate the Council's Financial Strategy and to inform any consequent decisions on capital investment and revenue savings plans to be taken by Full Council and Committees, while recognising the Council's duty to set a balanced budget, complying with relevant legislation.

7. REASON FOR THE DECISION:

To formulate the Council's Medium-Term Financial Strategy and set the financial context and framework for decisions to be taken by the Council.

8. BACKGROUND PAPERS:

None.