ITEM 9 Medium Term Financial Strategy 2019/20 – 2021/22

Report of the Finance Portfolio Holder

Recommended:

1. That the Medium Term Financial Strategy (MTFS) for 2019/20 to 2021/22 be approved.

2. That the Medium Term Financial Forecast outlined in Annex 3 be noted.

3. That the delegated action taken by the Chief Executive detailed in paragraph 5.7 be noted.

SUMMARY:

- This MTFS sets out the framework within which the 2019/20 budget will be prepared.
- It also sets out the Medium Term Financial Forecast for the General Fund Revenue Budget together with details of Revenue savings, which will form the basis of the 2019/20 budget.

1 Introduction

1.1 The Constitution sets out the processes for preparing the Council's budget. The Cabinet is required to consult with Members and other Committees in formulating the budget proposals to be presented to Council.

1.2 The MTFS sets out the key financial assumptions that have been made in producing the Medium Term Financial Forecast and sets out a proposed framework within which to work over the life of the plan.

1.3 It should be stressed that all of the options and assumptions in this report, relating to any potential budget changes, are for indicative planning purposes only. Final decisions on the overall Budget and Council Tax Level will not be made until February 2019 once the Local Government Finance Settlement has been announced. These decisions can only be made by Full Council.

2 Background

2.1 This MTFS complements the Council's Corporate Plan and sets out a clear framework for financial decision making. The Corporate Plan makes clear what the Council's priorities are, and the MTFS sets out how the financial management process will contribute to delivering these priorities.

2.2 The MTFS has been produced at a challenging time for the Council's finances. The Council has a balanced budget and reserves are at a safe level – but there is little room for manoeuvre and savings will be required in future to maintain financial stability. The Government and the public expect that Council Tax increases are kept to a low level and the Council is committed to achieving this. At the same time, expectations on the Council to provide efficient and effective services have never been higher.

2.3 2013 saw a radical change in the world of local government funding. Localisation of business rates and of support for council tax has had a profound effect on local authority finances and the level of funding risk that individual authorities face. The implications of these changes have been and continue to be monitored carefully to ensure that any adverse financial impacts are addressed as soon as possible.

2.4 Universal Credit will replace a number of means tested benefits for working age residents including Housing Benefit. On 4 July 2018 the Universal Credit Full Service was rolled out to the remaining Jobcentres in the Test Valley area which means the gateway to new claims for Housing Benefit for most customers living in the Borough is now closed. The Council will continue to assess claims for Council Tax Support and some Housing Benefit claims (including customers living in temporary or supported accommodation, households with more than two children and pensioners). All existing legacy benefits including Housing Benefit cases for working age customers will migrate to Universal Credit between July 2019 and March 2022. There is likely to be a significant reduction in the workload of the benefits team as cases migrate to Universal Credit.

2.5 Funding levels for Local Government are falling rapidly and will continue to do so as the Government tackles the national deficit. Revenue Support Grant will disappear in 2019/20, the new conditions attached to New Homes Bonus means that this will reduce as a resource in future, and councils expect a reduction in the level of retained business rates from 2020/21 onwards as the system is reset. So far, the Council has responded by “doing things differently” and by finding efficiencies, savings and raising additional income where it can without affecting front-line services.

2.6 This MTFS includes a forward look over the next 3 years, to anticipate additional spending requirements, and the level of savings that will be needed to keep Council Tax affordable. By anticipating financial pressures now, the Council will be in a better position to meet the challenges ahead in a way that ensures financial resources are targeted to the Council’s highest priorities.

2.7 However, this strategy comes with a strong health warning as it is not possible to forecast with absolute certainty how the changes in local government funding will pan out. The post election fall-out has left local government more uncertain than ever about the future of funding for the sector. The uncertain outcome of the election, and particularly the fall of the Local Government Finance Bill, has made it unclear whether the government will go ahead with key policies or change direction on others.

2.8 The financial forecasts that follow are based on a credible analysis of the potential options, but the potential outcomes are inherently uncertain without answers to four key questions:

(a) Will the Government mitigate the effects of a reset in the Business Rates Retention Scheme as it moves from a 50% to 75% retention basis?

(b) What funding settlement will local government get after the end of the current four-year guarantee?

(c) Will further changes be implemented to the New Homes Bonus?

(d) How will the Government implement the Fair Funding Review?

2.9 The MTFS forecasts will be revised at least annually to reflect the most up to date issues, priorities and pressures faced by the Council. Further information on any aspect of the Council's finances can be obtained from the Council's website.

3 Financial Management Principles

"Investing in Test Valley…is about devoting our energy, skills and resources to achieving the best results for our residents and communities across the Borough." – "Investing in Test valley" Corporate Plan 2015-2019 and beyond.

3.1 The Council has a duty to the public for responsible use of their money. The Council will at all times conduct its financial affairs in a prudent, responsible manner, but in a way that encourages innovation, achieves improvement and facilitates partnership.

3.2 The following specific principles underpin the Council's financial management arrangements:

(i) The Council will conduct its financial management with integrity, probity and in accordance with the standards and expectations of a publicly funded body.

(ii) The Council will ensure that budgets are aligned to the Corporate Plan and based on realistic estimates.

(iii) The Council will work with partners in the public, private and voluntary sectors to maximise funding available to deliver strategic priorities.

(iv) The Council will base its decision making upon complete, reliable and timely financial information, and a full evaluation of all the financial and risk implications.

(v) The Council will ensure that ongoing funding is available before recruiting new staff and will make use of temporary appointments where this will meet business needs.

(vi) The Council will secure value for money and have regard to environmental considerations in the procurement of supplies and services and will improve the efficiency and effectiveness of its procurement process. To encourage better procurement practice there will be no inflationary increases in budgets for supplies and services (except when there is a contractual obligation to apply indexation).

(vii) The Council will maximise its income and will increase its fees and charges by at least the rate of inflation except where strategic aims, legal requirements, contractual obligations or market forces would render this inappropriate.

(viii) The Council will hold its managers accountable for remaining within their budgets, but will empower managers to take the business decisions necessary to do so.

(ix) Before committing to additional expenditure, the Council will ensure that additional funding, improved income and/or savings are identified to meet the extra costs.

(x) The Council will maintain balances and reserves to enable the Council to respond effectively to unexpected events and opportunities, and sufficient to meet all known future liabilities.

(xi) The Council will identify savings to support budgetary pressures and not use its general balances; however, use of earmarked reserves may be made to fund specific or one-off items where appropriate.

(xii) The Council will ensure that its published financial information is reliable and understandable.

4 Budget Strategy

Financial Strategy Aims

4.1 The Council's financial aims for the period covering the next three years are set out below. These aims are described in detail in this report and form the overarching aims for each budget setting year within the financial strategy period.

- To maintain a low Council Tax whilst delivering high quality frontline services.
- To ensure that the efficiency culture remains embedded within the Council, systematically challenging and securing Value for Money.
- To ensure that the Council's resources continue to be focussed on meeting the Council's Vision for Test Valley and achieving its aims and priorities.
- To ensure that the Council's infrastructure is fit for purpose and that new capital needs are identified and met.
- To ensure that the Council's core ongoing financial position remains stable and continues to support the Council's key aims.
- To continue to seek out new investment opportunities through Project Enterprise, making better use of cash resources to enhance revenue returns.

Budgetary Assumptions

4.2 The budget over the duration of this Strategy is based on the following assumptions:

Revenue

(a) No Revenue Support Grant (RSG) being received after 2018/19.

(b) A full review of the Council Tax Support Scheme in 2018/19 to take account of Universal Credit entitlement.

(c) The Test Valley element of Council Tax being frozen for 2019/20.

(d) The Andover Levy being pegged to the movements in Council Tax over the medium term.

(e) A general zero inflation allowance for all expenditure budgets except for contractual obligations and a possible staff pay increase.

(f) The minimum level of working reserves is maintained at £2m over the financial strategy period.

(g) The Council continues to make cashable efficiencies every year.

(h) No growth bids will be entertained until the strategy is reviewed in July 2019 – i.e. all growth pressures (except the items detailed in Annex 6) will be managed by Heads of Service within existing budgets or met from earmarked reserves where this is appropriate.

(i) No in-year supplementary estimates will be approved by the Cabinet, although a small contingency provision will be available to meet exceptional or extraordinary items of expenditure.

(j) No increases in Car Parking charges for 2019/20.

(k) All other income will be maximised by thorough fees and charges' reviews. These are expected to be increased by a minimum of inflation, or such increase as the individual markets can bear except where strategic aims, legal requirements, contractual obligations or market forces would render this inappropriate.

(l) New Homes Bonus to decrease over the next three years from 2019/20 to 2021/22. This element of financing to be used for specific purposes as follows:

- Topping up the Community Revenue Fund as necessary
- Annual contribution to the Community Asset Fund
- Capital financing of assets with a community benefit e.g. Playground improvements
- Offset to the expected continuing reductions in Government financial support

More details of this budget assumption are set out in paragraph 4.12.

Capital

4.3 The Council will maximise the utilisation of, and rate of return on, the assets it holds on its balance sheet.

4.4 All capital expenditure will be funded in accordance with the principles contained in the Prudential Code for Local Authority Capital Finance. All decisions on capital expenditure to be taken so that investment is prudent, sustainable and affordable, and that the full implications of all capital expenditure decisions are taken into account in the Council's Revenue Budget.

4.5 See separate annex 7 for the details of the Capital Strategy.

Review of Reserves

4.6 Reserves are held for a variety of different reasons. Some relate to known and relatively certain future costs such as a planned building maintenance, vehicle and IT replacement. Others concern possible, though less certain, liabilities such as unexpected additional costs, or a sudden drop in income from fees and charges. This is where one moves into questions of judgment and prudence.

4.7 Reserves are a hedge against risk. Demand for public services is increasing at the same time that the Government is putting a squeeze on public expenditure. Though predictable in general terms, these trends are difficult to quantify and forecast precisely. Reserves provide a fall-back if there is a gap between the assumptions made in the budget and the trends which actually emerge.

4.8 The Corporate Challenge process has been very successful over the past eight years in challenging all aspects of the Council's spending, but as the Council approaches the next budget round for 2019/20, opportunities to find further savings and efficiencies are becoming harder to identify. In previous years, the Council has managed to balance the budget and protect frontline services through a mixture of savings, efficiencies, shared services, additional income and taking only a limited amount from reserves.

4.9 It is inevitable that if councillors wish to continue to protect services, they will need to draw down a larger element of reserves than in previous years. In doing so, they will need to exercise great care, including working through medium and long term consequences.

4.10 The nature of most local services is that they require recurring funding to meet staff and running costs year after year. Reserves are a one-off, finite source of funding. They can cover a shortfall in recurring funding for a specific period but, after they have been exhausted, the underlying shortfall will still be there. To solve the problem, services will need to be adjusted to a level which is affordable within the envelope of funding available.

Reserves as at 31/3/18

	31/3/17		31/3/18	
	£000s	£000s	£000s	£000s
Usable Reserves				
General Fund Balance	2,000		2,000	
Revenue and earmarked Reserves	22,352		23,813	
Capital Receipts Reserve	18,658		10,974	
Capital Grants Unapplied	377		1,163	
Total Usable Reserves		**43,387**		**37,950**
Unusable Reserves				
Revaluation Reserve	16,287		17,201	
Capital Adjustment Account	148,033		159,603	
Deferred Credits	7		7	
Collection Fund Adjustment Account	795		1,221	
Accumulated Absences Account	(178)		(178)	
Pension Fund Reserve	(55,900)		(58,520)	
Total Unusable Reserves		**109,044**		**119,334**
Total Equity		**152,431**		**157,284**

4.11 The Council's reserves are classified as either "usable" or "unusable".

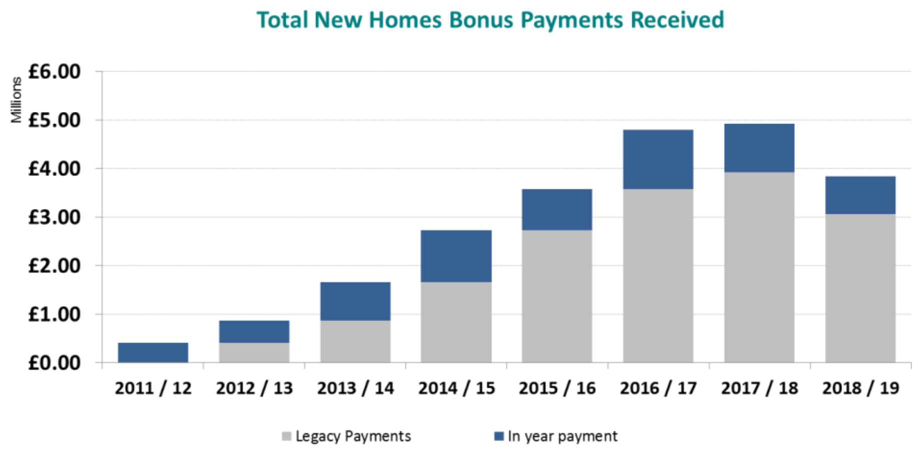
4.12 Usable reserves include the unallocated General Fund Balance, Earmarked Revenue Reserves, Capital Receipts Reserve and the Capital Grants unapplied Reserve. These are cash-backed reserves that the Council can apply to future expenditure subject to statutory conditions (e.g. the Capital Receipts and Capital Grants Reserves can only be used to finance capital expenditure).

4.12.1 The ***General Fund Balance*** represents a working balance to help cushion the impact of uneven cash-flows and minimise unnecessary temporary borrowing. It is reviewed annually by the Head of Finance and, based on the forecast cash-flows identified in the Council's Medium Term Financial Strategy, councillors are recommended to retain a prudent minimum balance in the General Fund. Currently, this is £2M.

4.12.2 ***Earmarked Reserves*** are a means of building up funds to meet known or predicted liabilities. The Council currently has twenty-four earmarked reserves totalling £23.8M. These are shown in more detail on page 59 of the Council's Statement of Accounts.

4.12.3 The largest earmarked reserve the Council carries in its balance sheet is the ***New Homes Bonus Reserve***. The New Homes Bonus is a grant paid by central government to local councils for increasing the number of homes and their use. The New Homes Bonus is currently paid each year for 4 years. It is based on the amount of extra Council Tax revenue raised for new-build homes, conversions and long-term empty homes brought back into use. There is also an extra payment for providing affordable homes.

4.12.4 The Council has been very successful in attracting New Homes Bonus. Actual and forecast amounts received and due, amount to over £33M in the eleven year period up to 2021/22. So far £17.1M has been committed from the NHB Reserve. With a further £1.3M being recommended to be drawn from the reserve over the medium term, this will leave a projected balance of £14.6M available by 31st March 2022 if the Scheme continues in its present format. Details of actual and forecast receipts are shown below:



New Homes Bonus Forecast (£m)	2019/20	2020/21	2021/22
2016/17 actual allocation	1.221		
2017/18 actual allocation	0.992	0.992	
2018/19 actual allocation	0.774	0.774	0.774
2019/20 forecast allocation	0.735	0.735	0.735
2020/21 forecast allocation		0.820	0.820
2021/22 forecast allocation			0.820
One-off adjustments			
Total each year (£m)	**3.722**	**3.321**	**3.149**

4.12.5 ***Capital receipts*** from the disposal of assets are treated in accordance with the provisions of the Local Government Act 2003. The Capital Receipts Reserve can only be used to fund capital expenditure, to repay debt (this council is currently debt-free), or to fund credit arrangements subject to the de minimis level set out in the relevant regulations (currently £10,000). A large proportion of the cash held in this reserve came from the LSVT of Council housing stock on 27 March, 2000. At the time, it was recognised that the Council would have additional residual costs to bear following the formal transfer of assets and winding up of the Housing Revenue Account. Interest earned on these capital receipts has therefore been used (and continues to be used) to help offset these costs and achieve a balanced budget.

4.12.6 The ***Capital Grants Unapplied Reserve*** holds the grants and contributions received towards capital projects for which the Council has met the conditions that would otherwise require payment of the monies, but which have yet to be applied to meet expenditure. The balance is restricted by grant terms as to the capital expenditure against which it can be applied.

4.12.7 The Head of Finance has carried out a detailed review of the Council's usable reserves and looking at current levels of balances, he considers that they will remain adequate for meeting the Council's needs over the medium term.

4.13 ***Unusable reserves*** contain technical accounting adjustments and, as the name implies, these reserves are not cash-backed and therefore cannot be used to finance expenditure.

5 Financial Context

Government Funding

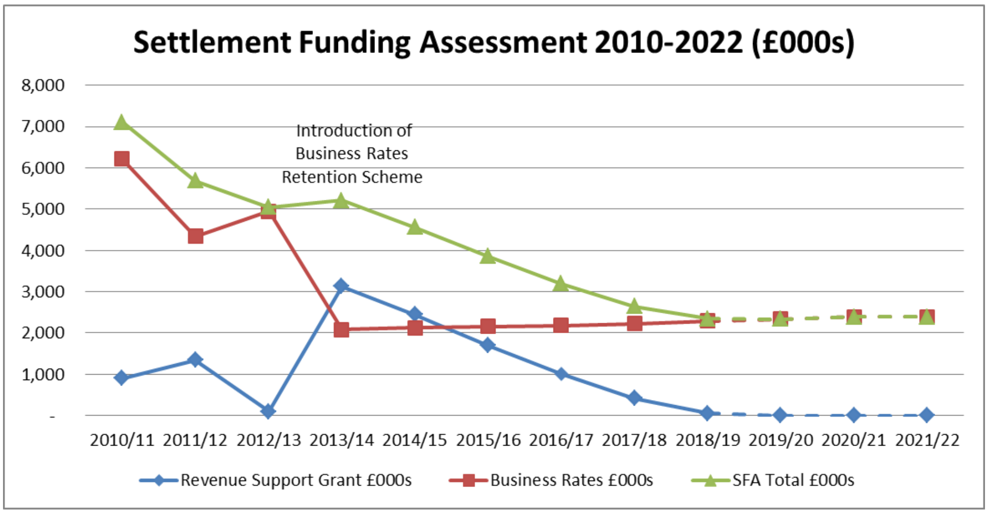
5.1 The Government's Comprehensive Spending Review (CSR) 2010 indicated that, over a four year period, funding would be reduced by 28% leading up to 2014/15. In fact, reductions were even more extreme than expected for most district councils including ours. In 2010/11, Government support through the Settlement Funding Assessment (SFA) totalled £7.1M. By 2014/15, SFA reduced to £4.6M, a reduction of £2.5M or 36%. Taking into account inflation, the reduction in Government support in real terms over four years was over 44%. By 2019/20, SFA is projected to be less than a third of the amount received in 2010/11, a reduction of £5.1M.

5.2 The Council's forecast of Government support for the next three years is shown below:

ACTUAL AND FORECAST LOCAL GOVERNMENT FINANCE SETTLEMENT					
Year	***Revenue Support Grant £000s***	***Business Rates £000s***	***SFA Total £000s***	***Change £000s***	***Change %***
2010/11	902	6,208	**7,110**		
2011/12	1,341	4,340	**5,681**	-1,429	-20.1%
2012/13	96	4,946	**5,042**	-639	-11.2%
2013/14	3,127	2,080	**5,207**	+165	+3.3%
2014/15	2,444	2,121	**4,565**	-642	-12.3%
2015/16	1,696	2,161	**3,857**	-708	-15.5%
2016/17	1,012	2,179	**3,191**	-666	-17.3%
2017/18	417	2,224	**2,641**	-550	-17.2%
2018/19	56	2,291	**2,347**	-294	-11.1%
2019/20	-348	2,341	**1,993**	-354	-15.1%
2020/21	+0	2,393	**2,393**	+400	+20.1%
2021/22	+0	2,393	**2,393**	+0	+0.0%

5.3 According to LGA figures, 168 councils – almost half of all councils made up of districts, counties, unitaries and London boroughs – will lose all RSG by 2019/20. This applies to Test Valley Borough Council and is reflected in the table above showing the double blow of losing grant and actually having to hand over £348,000 extra in local business rates income under "negative" RSG payments in 2019/20.

5.4 In its consultation paper issued on 24 July 2018, the Ministry of Housing, Communities and Local Government (MHCLG) stated that its preferred option for dealing with "Negative RSG" is simply not to make the tariff adjustments that are required for it to take effect. Although this will not be confirmed until the Local Government Finance Settlement later this year, the budget forecast in this report has been prepared on the assumption that the Government will proceed with its preferred option and that these extra payments will not be required. The £348,000 payment has therefore been removed from the forecasts as shown below:



Business Rates

5.5 The Business Rates Retention Scheme allows Councils to retain a proportion of any growth in business rates income over the baseline shown in the table and graph above. The forecasting of business rates income is especially difficult due to two factors:

(a) The impact of appeals arising from the national business rate revaluation in 2017/18, and

(b) The potential for further reform of the business rate system with Local Government retaining 75% of business rates income by the end of the current Parliament (subject to, as yet unknown, tariffs).

5.6 The budget forecasts in annex 3 are based on the current business rates system. This shows surpluses (ie. Business rates growth continuing over the medium term until 2019/20 when a full reset of the system is expected with a consequential loss of all accumulated growth at that point (ie. £2.3M). An update to these forecasts will be undertaken later in the year to assess how much of each year's surplus can safely be used to support the revenue budget.

5.7 In the meantime, Hampshire Councils have been exploring the benefits of pooling business rates across Hampshire. Following this work, the Chief Financial Officers of Hampshire County Council and all district councils unanimously agreed to submit an application to the Government to be considered for the Business Rates Pilot Scheme in 2019/20. This application had to be made by 25 September and following consultation with and support from Portfolio Holders and at the recommendation of the Head of Finance, the Chief Executive used his delegation to approve the bid as an urgent item. The outcome of the bid will not be known until November at the earliest, but if successful, it is expected that Hampshire as a whole would be able to retain an extra £26M of business rates income and this Council's share of this one-off windfall would be in the region of £1.7M.

Council Tax

5.8 With the continuing decline in Government support, Council Tax is now one of the Council's main sources of income. Consequently, there is an ever increasing strategic importance to the annual debate about whether to increase Council Tax and, if so, by how much.

5.9 The financial strategy aims to keep Council Tax at a low level taking into account spending priorities and Central Government funding. This should be set in the context of Central Government's expectations of local authorities and already very low levels of Council Tax charged in the borough. The Council Tax for Test Valley Borough Council was frozen at £121.41 in 2011/12 and again in 2012/13. In 2013/14, the Government recognised the problems created by being a low tax authority and made a special dispensation to allow those councils in the bottom quartile to put up Council Tax by £5. The Council took advantage of this offer and approved an increase of 4.1% to £126.41. The Council Tax was frozen again in 2014/15 and in 2015/16, and then increased by £5 for 2016/17, 2017/18 and again in 2018/19. The current level of Council Tax at £141.41 is still very low - the 26th lowest out of the 201 district councils in England, and the 4th lowest in Hampshire. It is also £43, or 23%, lower than the average Council Tax payable in the rest of England.

5.10 The MTFS forecast assumes that Council Tax will be frozen in 2019/20. The Government has not yet announced its council tax referendum threshold for 2019/20, but this is likely to be the same as last year (as outlined in the MHCLG's recent consultation paper: July 2018) allowing the Council to increase its Council Tax by up to £5 without triggering a referendum. The table below illustrates that the Government looks likely to continue to make this concession up to 2019/20 and has in fact built this higher increase into its own estimates of the Council's "spending power".

Illustrative Core Spending Power of Local Government;	2015-16	2016-17 £ millions	2017-18 £ millions	2018-19 £ millions	2019-20 £ millions
Settlement Funding Assessment*	3.9	3.2	2.6	2.3	2.0
Council Tax of which;	6.0	6.4	6.8	7.2	7.6
Council Tax Requirement excluding parish precepts (including base growth and levels increasing by CPI)	*6.0*	*6.2*	*6.5*	*6.8*	*7.1*
additional revenue from referendum principle for social care	-	-	-	-	-
additional revenue from £5 referendum principle for all Districts' Band D Council Tax level	-	*0.2*	*0.3*	*0.4*	*0.5*
Improved Better Care Fund	-	-	-	-	-
New Homes Bonus	3.6	4.8	4.8	3.0	2.9
Rural Services Grant	-	-	-	-	-
Transition Grant	-	0.1	0.1	-	-
Core Spending Power	**13.5**	**14.4**	**14.3**	**12.5**	**12.5**
Change over the Spending Review period (£ millions)					-1.0
Change over the Spending Review period (% change)					-7.6%

5.11 Freezing Council Tax in 2019/20 has been made possible due to the Council's continued drive to generate additional income from other sources as the Government has reduced its financial support to local authorities. Income derived from three main sources has enabled the Cabinet to recommend a freeze next year:

(a) Continued growth in Business Rates income. Test Valley Borough Council is a business-friendly Council and it is not surprising that over the last five years it has achieved the highest level of retained business rates income growth in Hampshire reflecting the amount of new businesses attracted to the Borough;

(b) The new Leisure Contract will generate additional net income of £783,200 next year as new facilities open and older ones are refurbished;

(c) Project Enterprise returns from commercial property investments add significantly to the Council's financial stability. Estimated income from this source is expected to be £1.9M in 2018/19 and over £2M in 2019/20.

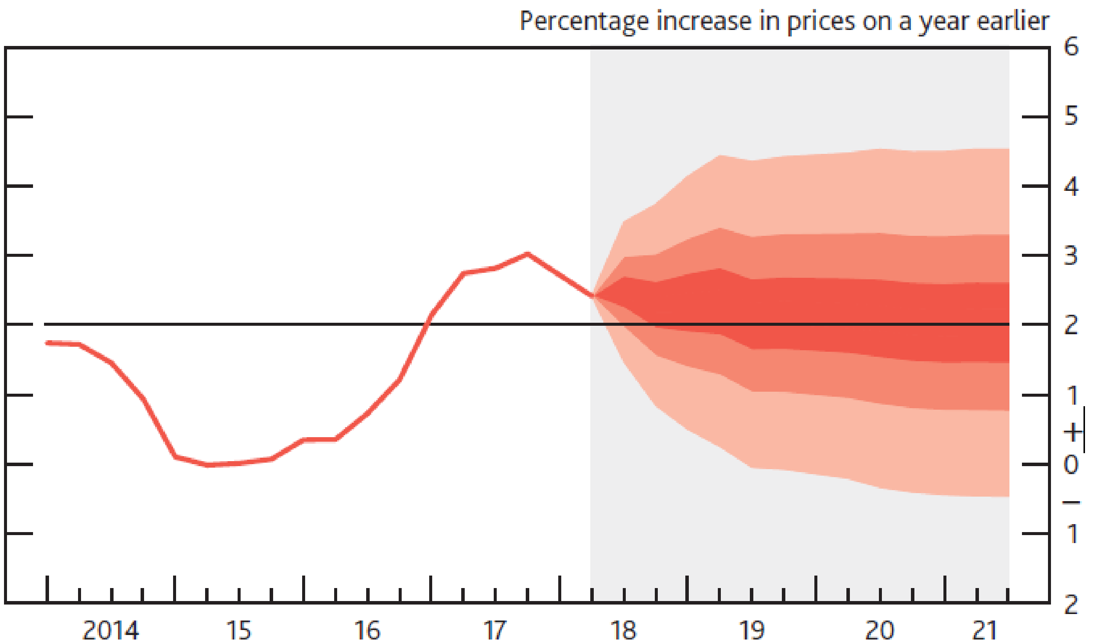
5.12 The proposed freeze will “cost” the Council £240,000 in income forgone, but clearly demonstrates the ongoing commitment to meeting the strategic aim of “maintaining a low Council Tax whilst delivering high quality frontline services”.

6 Key Budget Pressures and Influences

Pay and prices

6.1 The largest source of cost pressure comes from inflation. In order to maintain price stability, the Government has set the Bank of England’s Monetary Policy Committee (MPC) a target for the annual inflation rate of the Consumer Prices Index (CPI) of 2%. Though energy prices have been raised recently, consumer price inflation is expected to fall back below the 2% target level as the post-referendum fall in the value of Sterling dissipates. CPI has been trending lower for the last seven months, and has further to go as the fall in import prices continues to feed into lower CPI goods inflation. There are some upside pressures to note, with oil prices rising and that should underpin inflation in the short term as petrol and utility prices react.

6.2 Pay and price inflation allowances have been built into the budget forecasts equating to approximately £600,000 p.a. This is in line with the central forecasts produced in the Bank of England Inflation report (August 2018). However, this CPI inflation projection is based on the assumption that the Bank Rate will reach 1.1% by mid-2021, so may need revising later in the year.



Revenue impact of the Capital Programme

6.3 The capital programme is currently financed through a combination of capital receipts supplemented by specific grants and contributions. The balance on the Capital Receipts Reserve at 31 March 2018 was £11.0M. It is expected that the Capital Receipts Reserve will be fully committed by the end of 2018/19 and the Council will be using a mixture of internal borrowing and borrowing from the Public Works Loan Board (PWLB) to finance further capital expenditure. This practice is allowed in accounting regulations and is in line with the limits set in the Council's Treasury Management Strategy Statement (approved by Council, February 2018).

6.4 Further investments are expected through Project Enterprise that may also require the use of prudential borrowing. Each £1M of borrowing is estimated to cost in the region of £79,000 p.a., although the cost is dependent on the prevailing rate of interest, the type of loan and the term of the loan when the asset is acquired. (Estimates based on a 2.21% interest rate annuity loan over 15 years).

Interest Rates

6.5 The Council's Treasury Adviser, Link Asset Services, has provided the following forecasts of interest rates:

	End Q3 2018	End Q4 2018	End Q1 2019	End Q2 2019	End Q3 2019	End Q4 2019	End Q1 2020	End Q2 2020	End Q3 2020
Bank Rate	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%
5yr PWLB Rate	2.00%	2.00%	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%
10yr PWLB Rate	2.40%	2.50%	2.50%	2.60%	2.70%	2.70%	2.80%	2.90%	2.90%
25yr PWLB Rate	2.80%	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%
50yr PWLB Rate	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%

6.6 Link Asset Services undertook its last review of interest rate forecasts at the end of August 2018 after the quarterly Bank of England Inflation Report. There was no change in overall MPC policy at that meeting, but the Bank of England raised interest rates in August because it believed the economy was running close to full capacity, which risked causing inflation to continue overshooting its 2% target even taking into account the effect of sterling's weakness. The current interest rate of 0.75% is the highest since March 2009.

6.7 However, the MPC meeting of 13 September revealed a sharp change in sentiment. The Bank of England has now warned of the mounting risks to the British economy from a no-deal Brexit, with firms already putting investments on hold. As the Bank's nine-strong monetary policy committee (MPC) voted unanimously to keep rates on hold at 0.75%, it warned there had been increasing signs of stress linked to Brexit since its last meeting just a month previously. Given these warnings, the money markets are now expecting interest rates to be left on hold until at least August 2019.

6.8 On 19 September, the ONS released data which showed that UK inflation rate had risen unexpectedly in August to 2.7%, the highest level in six months. Economists had expected a Consumer Prices Index rate of 2.4% and this will come as unwelcome news to the Bank of England, as they will want to leave policy unchanged until there is some clarity over Brexit and will not want to be forced into a rate rise by accelerating prices.

6.9 The MTFS forecast is based on base rate levels as shown in the table in paragraph 6.5 above. Further work is currently being carried out to assess the likely cashflows expected in 2019/20 and beyond. A further update will be provided to Cabinet in January and February using the latest market information.

Leisure Contract

6.10 The new leisure contract with Places for People started on 1 April 2017. This is forecast to bring significant net revenue benefit to the Council over its 30 year life, and as such is expected to strengthen the Council's overall financial position in the medium and longer term. Savings have been built into the medium term forecast as set out in the contract. This will need to be kept under review in the coming years as the contract moves from its construction/refurbishment phase to its operational phase.

Welfare Reform

6.11 As mentioned in paragraph 2.4, Universal Credit Full Service is now live in the Test Valley area. Full migration to the new system is not now expected to be completed until 2021/22. The resources in the Revenues team are currently undergoing a full review with a view to implementing a new structure from 1 April 2019. A number of unfilled posts have been deleted from the Council's establishment and all temporary contracts ended. Levels of staffing will be kept under review along with the current Administration Grant. The Government has deferred making a decision regarding the administration of Housing Benefits for Pensioners; changes are now unlikely to be implemented within this Parliament.

6.12 The results of the Service review will be factored into the MTFS at the appropriate time. The Council will need to monitor the position carefully and accept that there may be a risk of increased expenditure which will need to be dealt with in future.

Hampshire County Council's "Transformation to" Savings Proposals

6.13 Hampshire County Council's plans to transform its budget over the medium term include proposals to reduce its overall revenue budget by £140M (Transformation to 2019) and by a further £80M (Transformation to 2021). Work continues to assess the impact of these budget reductions and what they might mean in practice for Test Valley residents. It is difficult to assess the potential financial implications until further details of the proposals become available, but reductions of this magnitude will undoubtedly have a knock-on effect to this Council's budgets that will have to be carefully monitored and managed.

6.14 No additional costs in relation to these proposals have been included in the medium term financial forecasts at this stage of the budget process.

7 Overall Revenue Budget Summary

7.1 The Revenue Forecasts for 2019/20 to 2021/22 have been drawn up at a macro level. They do not constitute detailed budgets, which will continue to be prepared on an annual basis within the normal timescales. However, the costing of specific issues and evaluation of proposed developments has informed the forecast.

7.2 The forecast is based on a middle case scenario using the assumptions shown in annex 2. It should be recognised that there will not be sufficient resources to meet all the service delivery ambitions and priorities of the Council without the generation of significant savings or additional income. This financial strategy for the three year period to 2021/22 should ensure that the financial resources of the Council continue to be aligned to the delivery of the Council's service and organisational priorities.

7.3 Achieving the improvements that the Council has set itself will require difficult policy decisions and resource choices to be made.

7.4 The budget principles and guidelines outlined in this strategy will allow for a phased use of reserves over the medium term to allow time to adjust to a standstill budget and an ever decreasing amount of external support. The corporate challenge process has identified significant savings and additional income of £343,430, and the proposed use of retained Business Rate growth will help the budgetary position in the short-term. The current budget gap for 2019/20 is £50,300 rising to £835,000 in 2021/22. The savings and additional income options being put forward for consideration are shown in annexes 4 and 5.

7.5 Current projections indicate the following financial position:

Revenue Budget Summary Statement 2019/20 - 2021/22

	Para. Ref.	2018/19 £000s	2019/20 £000s	2020/21 £000s	2021/22 £000s
Base budget		**12,908.4**	**12,908.4**	**12,136.4**	**9,810.5**
Base changes			(89.9)	(40.3)	20.0
Annual Inflation	6.1		590.0	600.0	600.0
Additional Income:					
Net income from new leisure contract	6.10		(783.2)	(344.2)	379.8
less: Financing costs			(1.0)	(1.0)	(1.2)
Renewable energy NDR growth			(7.0)	0.0	0.0
Investment Income			(88.8)	0.0	0.0
Corporate challenge income	Annex 5		(219.0)	(5.0)	(5.0)
Increased Costs:					
Reduction in New Homes Bonus	4.12.4		114.1	400.7	172.0
Unavoidable revenue pressures	Annex 6		286.0	0.0	0.0
Reduced Costs:					
Business Rates Levy			(340.4)	(1,590.8)	0.0
Asset Management Plan	Annex 6		0.0	(900.0)	0.0
Corporate challenge savings	Annex 4		(124.4)	0.0	0.0
Reserves:					
Reduced transfer to reserves			(108.4)	(545.3)	(172.0)
Draw from Pension Equalisation Reserve	7.8		0.0	100.0	0.0
General Fund Requirements		**12,908.4**	**12,136.4**	**9,810.5**	**10,804.1**
Financed by:					
Revenue Support Grant	5.2	(56.0)	0.0	0.0	0.0
Locally retained Business Rates Baseline	5.2	(2,290.6)	(2,341.4)	(2,392.9)	(2,392.9)
Locally retained Business Rates Growth	5.6	(2,946.0)	(2,265.1)	0.0	0.0
Share of Collection Fund Balance		(520.3)	(384.4)	0.0	0.0
Council Tax	5.10	(6,798.9)	(6,798.9)	(7,039.2)	(7,279.6)
Special Expenses Levy	4.2 (d)	(296.6)	(296.6)	(296.6)	(296.6)
Total Financing		**(12,908.4)**	**(12,086.4)**	**(9,728.7)**	**(9,969.1)**
Budget Gap		**0.0**	**50.0**	**81.8**	**835.0**

7.6 Details of further efficiency and other savings are currently being gathered together for Members' consideration in terms of the funding gap identified above and these will be presented to Cabinet in January 2019. The Cabinet will then decide on which options should be taken forward as recommendations to full Council as part of the budget setting process in February 2019.

7.7 The Council has a number of earmarked reserves set aside specifically to support the budget over the medium term:

- Budget Equalisation Reserve £682,000
- Income Equalisation Reserve £300,000

- Investment Income Equalisation Reserve £250,000
- Pension Equalisation Reserve £200,000

7.8 The budget forecast includes an assumption to draw the full £200,000 from the Pension Equalisation Reserve over this and next year (i.e. £100,000 in 2018/19 and £100,000 in 2019/20) to smooth the effects of an increase in employers' contribution rates with effect from 2018.

7.9 Whilst this will still leave an uncommitted balance of over £1M available to ease the pressure of balancing the budget during the next three years, it should be noted that this is not a sustainable solution to bridging the budget gap, as these reserves can only be used on a one-off basis.

7.10 The Council also has a Collection Fund Equalisation Reserve of £3.6M available to smooth the adverse effects of a Business Rates Retention Scheme reset in 2020. Current levels of forecast growth are £2.265M, so a hard reset, without any damping or transitional arrangements, could create a sudden financial shock to the Council. This Reserve would mitigate the impact and provide financial cover for 19 months allowing time to manage the reduction in external support.

8 Achieving the Medium Term Financial Strategy

8.1 It is anticipated that the required level of savings will be achieved through a combination of the following:

- Corporate Challenge process
- Procurement savings
- Improving value for money
- Service transformation
- Savings from partnership and shared services
- Generating additional income through use of fees and charges
- Generating additional income through external funding sources
- Generating additional income through Project Enterprise

8.2 However, it is inevitable that savings of this order can only be achieved by making difficult choices about the best use of limited and reducing resources and the relative priority of services offered to Council Taxpayers and stakeholders.

8.3 Annex 1 outlines the proposed action plan to achieve a balanced budget over the next three years.

9 Capital Strategy

9.1 The Capital Strategy has been reviewed and updated in light of this Medium Term Financial Strategy. The Capital Strategy sets out the following key principles:

(a) Linking together capital requirements related to corporate priorities for new projects and the ongoing capital need to maintain / repair existing assets through the Asset Management Plan

(b) Managing the approved Capital Programme in an affordable, financially prudent and sustainable way

(c) How new bids are introduced to the Capital Programme

(d) Monitoring progress against approved budgets

(e) Financing capital expenditure including borrowing requirements and Minimum Revenue Provision (MRP)

(f) Purchase of commercial properties and the resources required to ensure due diligence

(g) Knowledge and skills

9.2 Full details can be found in annex 7.

10 Corporate Objectives and Priorities

10.1 The Council's main aims are to ensure that the Borough remains a great place to:

- Live, where the supply of homes reflects local needs
- Work and do business
- Enjoy the natural and built environment
- Contribute and be part of a strong community

10.2 The Council will ensure that budgets are directed towards these key priorities. The mechanism for achieving this is the Council's Strategic Planning Framework (corporate clockwork), which includes a timetable for developing budgets and service plans to ensure that budgets are aligned to these priorities.

11 Consultations/Communications

11.1 The information contained in this report will form the basis for future discussions about the 2019/20 budget. It will go forward to Overview & Scrutiny Committee for comments.

11.2 The budget consultation with business will take place in the next three months. The final form of the consultation is not yet decided.

11.3 Once the provisional Local Government Finance Settlement has been received in late December it will be necessary to update the current figures and to take account of the comments made by the Overview and Scrutiny Committee and the views of businesses. It is planned to update the Cabinet with these figures and comments on 16 January 2019.

12 Risk Management

12.1 A risk assessment has been completed in accordance with the Council's Risk management process and has identified the significant (Red or Amber) risks shown below:

Risk	Likelihood	Impact	Management of Risk
Future resources less than assumed - **RED**	Significant **C**	Critical **II**	Revenue: Assess impact of Local Government Finance Settlement, the Fair Funding Review and the rest of the BRRS at the earliest opportunity. Monitor the impact of the localisation of business rates and of support for council tax and revise forecast as necessary. Capital: Schemes and projects kept on reserve list until resources are confirmed. Delay design stage approval of schemes in capital programme, if necessary. Monitor the amount of future usable capital receipts.
Savings anticipated from reviews are not delivered. - **AMBER**	Significant **C**	Significant **III**	Continue with corporate challenge and Service reviews. Closely monitor progress of budget / efficiency savings through monthly budget monitoring. Use of the Budget Equalisation Reserve if necessary.
Investment Income targets are not achieved - **AMBER**	Low **D**	Significant **III**	Review Treasury Management Strategy at least monthly. Quarterly meetings with Treasury advisors and Finance Portfolio Holder to look for low risk opportunities for investment. Use of the Investment Equalisation Reserve if necessary.
Legislative changes not anticipated. **- AMBER**	Significant **C**	Significant **III**	Keep up to date with Government policy and consultations, especially in relation to Universal Credit and the Fair Funding Review
Local data changes vary from those assumed. **- AMBER**	Significant **C**	Significant **III**	Review of assumptions with support from other bodies.
Pay awards or inflation vary from those assumed. **- AMBER**	Significant **C**	Significant **III**	These factors have a large influence on the revenue budgets. Pay awards to be agreed at an affordable level. Inflationary factors to be reviewed regularly.
Future spending requirements are under-estimated. **- AMBER**	Significant **C**	Significant **III**	Review Service Plans and spending projections. Closely monitor progress through budget/performance monitoring.
Revenue implications of capital decisions are not taken into account. **- AMBER**	Low **D**	Significant **III**	Capital Approval processes to be reviewed to ensure all revenue consequences continue to be identified.
Income targets are not achieved. **- AMBER**	Significant **C**	Significant **III**	Monthly monitoring of budgets and projections. Use of the Income Equalisation Reserve if necessary.
Staffing budgets are not sufficiently controlled. **- AMBER**	Low **D**	Critical **II**	Rigorous process is already in place for filling posts and managing vacancy targets.

Investment in priority areas does not lead to desired outcomes being achieved. **– AMBER**	Significant **C**	Significant **III**	Robust performance management framework incorporating quarterly monitoring reports.
Standards of service fall, particularly in non-priority areas. **- AMBER**	Significant **C**	Significant **III**	Robust performance management framework incorporating quarterly performance monitoring reports.
Increased demand for homelessness assessments and temporary accommodation - **AMBER**	Significant **C**	Significant **III**	Review the impact of Universal Credit rollout and the Homelessness Reduction Act additional responsibilities.
Adverse impact on service provision due to HCC's "Transformation to" savings proposals - **AMBER**	Significant **C**	Significant **III**	As further details of the proposals become available, assess the potential impact on service provision and take action to limit any financial implications.

13 Resource Implications

13.1 Resource implications are contained within the Strategy itself.

14 Legal Implications

14.1 The Council is required to set a robust and balanced budget under the Local Government Act 2003. This report is the first step towards achieving this aim for the 2019/20 budget.

15 Equality Issues

15.1 An EQIA screening has been completed in accordance with the Council's EQIA methodology and no potential for unlawful discrimination and/or low level or minor negative impact have been identified, therefore a full EQIA has not been carried out.

16 Other Issues

16.1 None.

17 Conclusion and reasons for recommendation

17.1 This MTFS takes account of all known financial implications and makes various assumptions in projecting the budget forward for the next three years.

17.2 The budget position outlined in the Medium Term Financial Forecast is not inconsistent with the position most other Local Authorities will face. However, significant savings will need to be found over the coming years.

17.3 These papers will now go forward to Overview and Scrutiny Committee for consideration. The next budget update will be in January, 2019.

17.4 The MTFS is recommended for approval for the following reasons:

- to ensure that the Council has a strategic approach to the management of its finances, and

- to enable available resources to be allocated to services in line with Council priorities over the medium term.

Background Papers (Local Government Act 1972 Section 100D) None			
Confidentiality It is considered that this report does not contain exempt information within the meaning of Schedule 12A of the Local Government Act 1972, as amended, and can be made public.			
No of Annexes:	7	File Ref:	N/A
(Portfolio: Finance) Councillor Giddings			
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Report to:	Cabinet	Date:	10 October 2018