

## **For publication**

### Quarter 2 Budget Monitoring 2018/19 & Updated Medium Term Financial Forecast

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Meeting: Council

Date: 12<sup>th</sup> December 2018

Cabinet Portfolio Deputy Leader

Report by: Director of Finance & Resources

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## **For publication**

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### **1.0 Purpose of report**

- 1.1 To provide the Council with an update on the budget position at the end of the second quarter, covering:
  - General Fund Revenue
  - Capital Programme
  - Housing Revenue Account
- 1.2 To meet the requirement in the Financial Procedure Rules to provide the Council with regular updates on the Council's financial position.

## **2.0 Recommendations**

- 2.1 To note the financial performance in the first half of the financial year and the new medium term forecast (Sections 4 and 6).
- 2.2 That the changes to the medium term forecast outlined in Section 4 are approved.
- 2.3 That the supplementary estimate for registration of electors detailed at para 4.2.7 be approved.
- 2.4 That the proposed use of reserves as set out in Section 5 of the report be agreed and the new application of funding in para. 5.2, 5.3 and 5.6 be approved.
- 2.5 To note the updated capital programme outlined in Section 7.
- 2.6 That the additions to the capital programme detailed in para 7.2 are approved.
- 2.7 To note the position on HRA budgets (Section 8).
- 2.8 To approve the indexation of the housing repairs contract from 2017/18 onwards (para 8.1).
- 2.9 To note the application for 75% Business Rates Pilot status for 2019/20 (Section 9).
- 2.10 That the budget preparation guidelines in para. 10.1 be approved.
- 2.11 That the approach to budget consultation be considered (para. 10.3).

### **3.0 Background**

- 3.1 The Council approved the original budget for 2018/19 on 22<sup>nd</sup> February 2018. The Band 'D' Council Tax was set at £159.89. The original budget for 2018/19 was a surplus of £56k.
- 3.2 All of the indications are that the medium term outlook will continue to be challenging. Any budget announcement for 2019/20 and future years will follow the release of the 2019 Spending Review. The Medium Term forecast approved by the Full Council on 22<sup>nd</sup> February 2018 showed increasing deficits of £291k in 2019/20 rising to £1m by 2021/22.
- 3.3 A revised surplus of £298k for 2018/19 was reported to members as part of the Month 2 Budget Monitoring 2018/19 & Updated Medium Term Financial Forecast report.
- 3.4 This report was considered at the Cabinet meeting on 23 October, 2018, where it was resolved that the recommendations at paragraphs 2.1 – 2.11 be approved by full Council.

### **4.0 Current Year's Budget**

- 4.1 We started month 3 of the year with a forecast surplus of £298k. At the end of the second quarter other variances have produced an anticipated deficit of **£130k**. A summary of the key variances is provided in the table below:

<b>2018/19 UPDATED BUDGET FORECAST - TO END OF QUARTER 2</b>		
Surplus Forecast at the start of the year		(56)
Changes reported at the end of Month 2		(242)
<b>Surplus Forecast at the start of Month 3</b>		<b>(298)</b>
<b><u>Budget Saving - increased income:</u></b>		
VAT Sporting Exemption – Leisure Facilities	(200)	
Covenant Release Income	(35)	
Industrial Units	(7)	
Legal Fees – Land Sales	(14)	(256)
<b><u>Budget Saving - reduced expenditure:</u></b>		
Refuse Collection Contract	(155)	
External Audit Fee	(5)	(160)
<b><u>Budget Increase - reduced income:</u></b>		
OSD Surplus	315	
Leisure Facilities	100	
Vicar Lane – Head Rent	69	
Town Hall – Rental Income & Service Charges	43	527
<b><u>Budget Increase - increased expenditure:</u></b>		
Leisure Facilities – Employee Costs	135	
2 Year Pay Deal Award	97	
Project T	33	
Dunston Hi-Tech Units – Business Rates	25	
Vacant Units		
ICT transfer in from Arvato	20	
By-Election Costs	5	315
Net of all other variances		2
<b>Updated Deficit Forecast</b>		<b>130</b>

## **4.2 Changes to Approved Budgets**

- 4.2.1** Following discussions with our external VAT advisors, the Council has recently informed HMRC of our intention to implement Sporting Exemption from VAT on our sports centres following the success of the London Borough of Ealing ruling against HMRC. This will be implemented from August 2018 and is expected to save £200k in 2018/19 and £300k p.a. in future years.
- 4.2.2** Employee costs at the two sports centres have risen and a few of the significant income streams have not achieved their expected levels. If this continues, the additional net cost of operating the sports centres will increase by £235k in this financial year. The assistant director is currently putting in place a number of measures to remedy this position.
- 4.2.3** The original medium term forecast included a surplus from trading by OSD of £255k. OSD are currently forecasting a trading deficit for 2018/19 due to reduction in housing repairs and the impact of this is a reduction in income this year of £315k. Housing and OSD are working towards the delivery of the original budgeted surplus.
- 4.2.4** During the summer the NJC two year pay award for employees was agreed. A provision of 2% had been included in the original budget for both years but due to the inclusion of significant increases for lower paid members of staff, a further £97k is required to fund the increase for 2018/19 rising to £178k next year.
- 4.2.5** A review of the refuse collection contract has highlighted an opportunity to reduce the budget by £155k.
- 4.2.6** Delays in tenants moving into the Town Hall and letting of Town Hall space has led to a decrease in rental income of £43k in 2018/19.

- 4.2.7 Changes to the procedures for registration of electors have increased costs by £38k p.a. These additional costs were initially met by government grant but this grant funding has now ceased. This additional spend therefore forms part of the base budget and a supplementary estimate is required to cover these ongoing costs from 2019/20 onwards.
- 4.2.8 The transfer of the ICT function from Arvato has increased revenue costs by £20k in 2018/19. This may increase further with the transfer of the HR function.
- 4.3 The first draft budget report for 2019/20, including revised estimates for 2018/19, will be presented to the Cabinet on the 18<sup>th</sup> December 2018. The draft budget report will provide a more up-to-date and comprehensive budget forecast.

## 5.0 Reserves

- 5.1 In addition to the General Working Balance, which is maintained at £1.5m, the Council operates a number of other reserves. Many of the reserves are earmarked and committed for specific purposes, such as property repairs and vehicle & plant replacements. There are two major reserves where the Council has wider discretion on how they are used – the Budget Risk Reserve and the Service Improvement Reserve.
- 5.2 **Budget Risk Reserve** – the Council maintains this reserve as a supplement to the Working Balance. It is also used to finance the severance costs arising from voluntary staffing reductions and the outcomes of service restructuring exercises. The table below shows the opening balance in the reserve at the start of the financial year and the currently approved or anticipated movements on the reserve. There is one new application to the fund to note:
1. Preliminary works for extension of industrial property portfolio.

<b>Budget Risk Reserve</b>	<b>Updated Forecast £'000</b>
<b>Balance b/fwd 1<sup>st</sup> April</b>	<b>683</b>
Less Approved Commitments:	
Transfers from other reserves	13
17/18 carry forward – Peak Resort business case	(30)
Tourism	(2)
Extension of industrial property portfolio	(20)
Skills Action Plan	(2)
Venues redundancy provision	(70)
Kiosk Payment Terminals x 3	(14)
D2N2 – enterprise advisor network	(11)
Pavements – rough sleeping solution	(25)
IDOX – reimbursement	39
<b>Uncommitted Balance</b>	<b>561</b>

5.3 **Service Improvement Reserve** – The table below shows the opening balance in the reserve at the start of the financial year and the currently approved or anticipated movements on the reserve. There is one new application to the fund to note:

1. Consultancy costs for a Green Waste strategy.

<b>Service Improvement Reserve</b>	<b>Updated Forecast £'000</b>
<b>Balance b/fwd 1<sup>st</sup> April</b>	<b>339</b>
Less Approved Commitments:	
Linacre Master Planning	(10)
HS2 Project Officer – 2yrs FTC	(62)
Former QPSC – business case	(5)
Green waste strategy	(30)
TPIC/DIC - Reimbursement	76
<b>Uncommitted Balance</b>	<b>308</b>

5.4 The uncommitted balances in these two major reserves are now £869k. There will be significant demands on these reserves to fund budget deficits, investment in transformation projects and to pay for severance costs from staffing restructures. The Cabinet should, therefore, continually review the commitments

against these finite financial resources to ensure that they are used in the most effective way.

- 5.5 **Safer surfacing of play areas** – It is proposed that £27k of monies set aside from Commercial Services historic trading surplus held in the DSO reserve be used to address some of the more immediate safer surfacing repairs with the work to be carried out during 2018/19. It is suggested that sites where the existing play equipment has some useful life will be prioritised.

## 6.0 Medium Term Outlook

- 6.1 The latest medium term forecast indicates increasing deficits in future years. The deficits beyond 2018/19 are challenging without officer and member plans to increase income, reduce costs and reduce net expenditure. The Council has a number of savings and income generation opportunities:
- Business plans reducing the venues and sport centre subsidies
  - Procurement savings
  - Tighter control on spending
  - Greater capital receipts through grants and asset disposals
- 6.2 However, the Council also faces a number of costs pressures on budgets including:
- Inflation on pay and non-pay costs
  - Business Rate appeals
  - Declining rents across our retail portfolio
  - Resourcing (staffing and resource) demands to deliver services
  - Government policy changes
  - Loss of all NHB and RSG
  - Impact of fairer funding review
- 6.3 The latest medium term forecast indicates significant deficits in future years. In 2018/19 the position has moved from a

£56k surplus to a deficit of £168k. The deficits beyond 2018/19 are a significant risk without continued officer and member decisions to reduce. Reductions to services may be necessary and tighter control on all capital/revenue spending as well as investment to raise income. The table below compares the latest forecast with the original budget forecast:-

	<b>Budget Forecasts</b>				
	<b>2018/19 £'000</b>	<b>2019/20 £'000</b>	<b>2020/21 £'000</b>	<b>2021/22 £'000</b>	<b>2022/23 £'000</b>
<b>February 2018 budget Deficit / (Surplus)</b>	(56)	291	848	1,010	1,000
Increase / (Decrease) Month 2	(242)	200	447	636	464
Increase / (Decrease) Quarter 2	428	294	173	159	166
<b>Latest Forecasted Deficit / (Surplus) Quarter 2</b>	<b>130</b>	<b>785</b>	<b>1,468</b>	<b>1,805</b>	<b>1,630</b>
Transformation Projects - Savings to be Achieved	-	-	100	100	100
Cease and Reduce Programme - Savings to be Achieved	25	53	53	53	53
CBC GF Properties - Business Rates Appeals	0	0	78	80	82
<b>Latest Savings Requirement</b>	<b>155</b>	<b>838</b>	<b>1,699</b>	<b>2,038</b>	<b>1,865</b>

## 7.0 General Fund Capital Programme

7.1 **Capital Receipts** - To date, £1.1m of capital receipts have been received during 2018/19. The original forecast for the year was £2.4m and included the rephasing of capital receipts for land at Ashgate Road, New Square and Poolsbrook. The current forecast of capital receipts for the year is £1.9m due to further rephasing of the Poolsbrook receipt. Further large capital receipts need to be identified by the Council beyond 2019/20 when the 'pipeline' declines, otherwise the Council's borrowing

will increase to fund further capital projects, putting more pressure on the General Fund deficits.

- 7.2 **General Fund Capital Spend** –the original capital budget for 2018/19 was £10m, this was increased to £15.5m in July 2018. The revised position now stands at £15.7m (see appendix A for details). The major differences in the capital programme are:
- Inclusion of works to Holland Road Play Area (70k), which is reaching the end of its useful life;
  - Inclusion of works to King George V Play Area (£50k) to be fully funded from grant;
  - Increase in costs of Beetwell Street car park (£200k) due to tender prices being higher than anticipated.

- 7.3 **Net Capital Financing** – The 2018/19 month 2 revised capital programme assumed a break even position and was approved by Council on 18<sup>th</sup> July 2018. The full amount of the Sheffield City Region Infrastructure Fund contribution towards the Northern Gateway schemes (£5.8m) was received in March 2018 in advance of the works, and this will allow the grant contribution to be applied in full in 2018/19 with a re-profiled CBC contribution occurring in 2019/20. Borrowing of £3.9m is required in 2018/19 and £1.4m in 2019/20 to fund Saltergate MSCP (£3m) and the increased capital programme. Repayment of prudential borrowing from capital receipts obtained in 2017/18 has been deferred in order to fund the increased capital programme. An updated capital programme will be reported to members in February 2019.

## **8.0 Housing Revenue Account (HRA)**

- 8.1 **Housing Revenue** - At the end of month 6, rental income was slightly ahead of target due to a reduction in void losses. The main expenditure items were on target, except for Housing Repairs where there was an underspend of £585k. The reasons for this large underspend are still being investigated, but it has adversely affected the OSD trading position, which is

now showing a deficit. However, there has been no indexation applied to the Repairs contract for 2 years (2017/18 and 2018/19) and approval is sought to reinstate indexation to this contract from 1<sup>st</sup> April 2017 based on the BCIS indices. This is calculated at 7.76% and will increase spend on Repairs by an estimated £543k in 2018/19 and also improve the OSD trading position. In addition, future repairs work will be at a higher rate. The revised figures will be incorporated into the HRA Revenue Budget which will be presented to Cabinet in February 2019.

**8.2 Housing Capital Programme** – A total of £3.8m has been brought forward from future year's budgets to fund external wall insulation (£1.4m) and new build schemes (£2.4m) in 2018/19. The latter is required in order to spend the retained "one for one" right to buy receipts. If these receipts are not spent they have to be returned to the Government plus interest. It is estimated that there will be an underspend of around £1.5m on current year's schemes due to delayed starts on site (Manor Drive new build) and reduced demand (Adaptations). The net impact of these changes is that capital expenditure is forecast to increase by £2.3m in 2018/19. This increase will be funded from the HRA Working Balance.

**8.3 HRA Business Plan** - The 30 Year HRA Business Plan is currently being reviewed to account for changes since the last version was presented to Cabinet on 19<sup>th</sup> December 2017. This includes the changes to Repairs spend highlighted above. The revised Business Plan will be presented to Cabinet at a future date.

## **9.0 75% Business Rates Pilot**

**9.1** MHCLG has recently invited applications from local authorities to become a 75% Business Rates Retention pilot authority for one year from 1<sup>st</sup> April 2019. The closing date for applications was 25<sup>th</sup> September 2018.

- 9.2 If the application is successful it would mean that half of the 50% share of business rate income which would go to central government would be retained within the pilot area.
- 9.3 Following our successful application for pilot status in 2018/19, Derby City Council has co-ordinated a bid for 2019/20 which includes the city, county and all district authorities in Derbyshire. Officers from all authorities have agreed the details of the bid. The chances of being successful again in 2019/20 are less as the amount of money to fund this initiative is lower so there will be fewer successful applications this year.
- 9.4 The outcome of the bid will be announced in the draft Finance Settlement expected in December 2018. If unsuccessful, the authorities included in the bid have indicated that they would wish to go back to the pooling arrangements in place for the financial year 2017/18.
- 9.5 The outcome of the bid will be reported to Cabinet at a later date. The current medium term forecast assumes that we will return to the pooling arrangements pre 2018/19.

## **10.0 2019/20 Budget Preparation Process**

- 10.1 The budget preparation process started in September when budget working papers and guidelines were issued to budget holders. The budgets are prepared on an 'incremental' basis i.e. taking last year's budget as the base and making adjustments for the following:
  - Variances that have been reported to and approved by the Cabinet.
  - Pay inflation – 2019/20 NJC pay award and an allowance of 2.5% per annum in future years.
  - Energy and property maintenance inflation as advised by the Facilities Maintenance Manager.

- Contract inflation as specified within contracts – assuming
  - RPI of 3.2% in 2019/20 and 3.5% in future years; and
  - CPI of 2.5% per annum.
- Business rates are based on the CPI in the previous September – a rate of 2.4% for 2019/20 and 2.5% in subsequent years is assumed.
- No inflation on other general items of expenditure including grants to voluntary organisations.
- Fees and charges increases – an average increase of 3% per annum for the period of the MTFP but only where it is considered that the market will bear such an increase.  
Fees and Charges reports will be submitted to Cabinet on the 13<sup>th</sup> November 2018.

These budget assumptions will be revised on a continual basis as we move through the budget process and as more up-to-date information becomes available. Cabinet is asked to note the budget setting guidelines.

#### 10.2 In terms of the Member reporting process:

- a) Quarter 2 budget monitoring and updated medium term forecast report for Cabinet (October) and full Council (December).
- b) Approval of the Localised Council Tax Support Scheme for 2019/20 to the full Council in December.
- c) Executive Member portfolio budget reports will be produced for consideration in early December.
- d) The Cabinet will consider the first draft budget in mid-December and the final budget report in February.
- e) The full Council will approve the final budget and council tax at the end of February 2019.

Updates will also be provided to the Overview and Performance Scrutiny Forum at key stages in the process.

10.3 Consultation with the public – it is proposed that we hold a one-off community assembly in January to facilitate consultation with the public with a similar format to previous years.

## **11.0 Risk Management**

11.1 Budget forecasting, particularly over the medium term, and in the current economic climate is not an exact science. Assumptions have to be made about possible changes where the final outcome could be very different e.g. government grants, pay awards, investment returns, etc. A full budget risk assessment will be included in the budget setting reports later in the year.

## **12.0 Legal Considerations**

12.1 There is a legal requirement for the Council to set a balanced budget before the start of each financial year and for the Director of Finance and Resources to report on the robustness of the estimates and the adequacy of the reserves. Clearly, there is a lot of work to be done over the coming months to be in a position to set a balanced budget for 2019/20 in February 2019.

## **13.0 Conclusions**

13.1 Work continues to identify savings and to raise income. Already officers are developing zero subsidy plans on venues and sports facilities, procurement savings, efficiency savings, cost control etc. We are still facing a budget deficit in the next financial year and escalating deficits in the years ahead. Officers and members will have to agree plans to reduce the deficits as under the Local Government Act 2012 the Council must provide a balanced budget. Decisions on where costs/services have to be reduced, investment focused and income raised will have to be continued by the Council to

formulate medium term plans. At the same time there are a number of risks that could add further pressure to the forecast deficits in future years e.g. Business Rates income, Universal Credit, Fair Funding, retail rents, inflation, staffing resource and the economy (Brexit).

## **14.0 Recommendations**

- 14.1 To note the financial performance in the first half of the financial year and the new medium term forecast (Sections 4 and 6).
- 14.2 That the changes to the medium term forecast outlined in Section 4 are noted.
- 14.3 That the supplementary estimate for registration of electors detailed at para 4.2.7 be approved.
- 14.4 That the proposed use of reserves as set out in Section 5 of the report be agreed and the new application of funding in para. 5.2, 5.3 and 5.6 be approved.
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- 14.10 That the budget preparation guidelines in para. 10.1 be approved.

14.11 That the approach to budget consultation be considered (para. 10.3).

## 15.0 Reasons for recommendations

- 15.1 To actively manage the Council's finances in the current financial year and forecast forward the emerging budget position to future financial years.

### Decision information

<b>Key decision number</b>	<b>756</b>
<b>Wards affected</b>	<b>All</b>
<b>Links to Council Plan priorities</b>	To provide value for money services.

### Document information

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<b>Background documents</b>	
These are unpublished works which have been relied on to a material extent when the report was prepared.	
<i>This must be made available to the public for up to 4 years.</i>	
<b>Appendices to the report</b>	
Appendix A	General Fund Capital Programme