



Charnwood Borough Council
Medium Term Financial Strategy
2010/11 to 2012/13

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I. Introduction

The Medium Term Financial Strategy (MTFS) reflects the financial position of the council based on the current Corporate Plan and service delivery aspirations in the medium term. The MTFS provides a high level assessment of the financial resources required to deliver the corporate objectives of the Council and considers how these resources can be provided within the financial context and constraints likely to be faced by Charnwood over the next three years.

The period covered by the MTFS is the three years ending 31 March 2013, which is one year longer than the current Corporate Plan.

The purpose of this document is to:

- Outline the principal factors that will influence the availability of the Council's financial resources in the medium term
- Inform and define the medium term service delivery plans of the Council in financial terms
- Present the options available to the Council, and set out the preferred solutions, in providing financial resources to deliver the Council's priorities as set out in the Council's Corporate Plan
- Set out the key financial policies that will underpin the Council's financial planning, budgeting and monitoring activities
- Inform the budget setting process for the 2010/11 financial year
- Provide the financial basis for the Council to decide its corporate priorities for future years.

This is a strategic document and should be read as such. In this document a certain amount of detailed budgetary information is presented but this should be regarded as indicative and illustrative. Whilst this document will inform the 2010/11 budget setting process it is natural that many of the figures quoted here will be amended and refined as the 2010/11 budgets are developed.

Scope of the MTFS

This strategy document covers all aspects of the Council's finances, such as revenue expenditure, income and Government grant support as well as addressing the availability of financial resources and the impact of the capital expenditure programme.

The Council has created an Arms Length Management Organisation (ALMO) to manage its housing stock. This operates independently of the Council but the financial impact of material ALMO activities are reflected in this document. In particular, there is an important relationship between the ALMO and the 'ring-fenced' Housing funding arrangements that remain within the direct ambit of the Council.

It should be noted that the finances of the Council are actively managed on an ongoing basis and that the adoption of this strategy will still require executive decisions to carry out any significant actions deriving from this strategy.

2. Executive summary

2.1 Strategic challenges

In common with many other Local and Central Government organisations Charnwood faces a challenging financial landscape.

At the present time there are numerous scenarios being put forward as to how this, and the following, government will address the financial issues it faces as a result of the unprecedented economic events over the last 18 to 24 months. At the time of writing, the indications are that government spending will continue at present levels for 2009/10 and that there will be cuts and reallocations of resources after that.

In addition, to the position with central government there is the continued uncertainty in the general economy. The continuing low level of activity in the property market affects the Council's revenue and capital income streams as there is lower income from Land Charges, Planning and Building Control fees plus there are fewer opportunities to sell surplus assets and utilise funds from Section 106 agreements with property developers. Whilst low inflation has a positive impact this is offset by reduced income from the Council's investments due to much lower interest rates and a limited range of suitable institutions with which to invest.

A further impact of the economic crisis has been the effect on the Council's pension scheme. The value of its assets and anticipated returns have fallen whilst the level of liability continues to rise primarily due to the increasing longevity of pensioners. In addition, many people in Charnwood have been affected by the downturn and this impacts adversely on their ability to pay Council Tax and council house rents, where relevant. This problem is also repeated in the corporate sector with there being a higher turnover of tenants in the council's industrial units plus higher arrears and bad debts.

2.2 Charnwood's challenges

As can be seen from the 'Central Case' set out in section 5, the General Fund is operating with an annual deficit of around £939k. Whilst this can be covered from reserves for the three year period, this is not sustainable going forwards. Accordingly, action must be taken to bring expenditure back in line with the council's income.

As explained above the ability to increase income is limited in the current economic environment and two thirds of the Council's income comes from central government grants and so cannot be increased unilaterally. Other charges are reviewed periodically and this will continue but it is unlikely that sufficient income can be raised to cover this shortfall. Therefore, the costs of service provision have to be reduced or the services cut.

For smaller shortfalls in the past reductions have been made by making 'across the board' reductions. This will not achieve the desired effect this time and in addition it can result in service provision falling below acceptable standards in many services rather than having a targeted number of services performing well within the

resources available. Some services have to be provided under statute whilst others are discretionary. The aim will be to decide which services will be delivered and at what level, as even statutory services can be provided in different ways. This prioritisation is underway and will inform the 2010/11 budget process.

The other major financial challenge of the Council is to rebuild its Housing Revenue Account balance. At the end of March 2009 this stood at £19k, or the equivalent of about £3 per dwelling. The Council would normally expect this balance to be around £110 per dwelling or £644k in total. This strategy assumes that this balance will be rebuilt to this level by the end of March 2013 through reducing costs and increasing the level of rental income by reducing rent losses through properties being empty.

3. Financial and economic context

The general financial situation of both the UK government and the UK itself have been widely covered in the media and this strategy will not go over this ground again.

The direct effects on Charnwood's finances are illustrated below by comparing income and costs in 2008/09 to 2007/08:

Planning and Building Control Fees	Down by £159k
Land Charges	Down by £161k
Interest Received	Down by £136k

There has been no material improvement in the first two of these items in 2009/10. The level of interest receivable continues to fall due to much lower interest rates and the more limited choice of institutions available to the Council. The budgeted decrease in interest receivable in 2009/10 compared with that actually received in 2008/09 is £1,232k and this estimate is in line with interest to date so far in 2009/10.

Another factor adversely affecting the Council's finances is the cost of Concessionary Travel. In 2008/09 the cost of the statutory element exceeded funding from central government by £160k. The costs will be higher in 2009/10 and future years with only limited increases in government funding so this gap will widen.

The downturn in the property market has also resulted in a sharp fall in the value of receipts from the sale of Council houses. On current trends the income available for Capital from this source will fall by £101k in 2009/10, following a fall of £478k in 2008/09.

Trends in Local Government are for increasing expectations of service delivery that must be satisfied in an environment where Central Government funding is static, or falling in real terms, and the Council's ability to maintain, let alone increase, its own revenue streams is very limited.

Overall, Charnwood Borough Council faces an extremely challenging financial landscape, in common with other Local Authorities, and this is reflected in the financial projections contained in this strategy.

4. Corporate planning and the capital plan

4.1 Corporate planning

The Corporate Plan outlines the Council's aims and objectives in the medium and longer terms, articulates the Council's service delivery aspirations and sets out how Charnwood will work together with partner organisations to deliver the range of services that the residents of Charnwood expect.

The Corporate Plan provides a framework from which individual service delivery and service enhancement plans, and the Capital Plan, are developed. The Council also develops a set of enabling or 'cross-cutting' plans, one of which is the Medium Term Financial Strategy, that underpin the service delivery and service enhancement plans. Other cross-cutting plans cover Equality and Diversity, Workforce, Property and Information Technology.

All of these plans inform, and are informed by, the MTFS and are developed on an interdependent basis to ensure that they reflect each other and provide a set of coherent, achievable and affordable plans to achieve corporate priorities.

4.2 Consulting with citizens and partner organisations

The Corporate Plan is the main vehicle by which the Council consults with citizens in order to develop its priorities, aims and objectives. Other plans, including the Financial Strategy, and also the Council's budget, are developed as enablers of the Corporate Plan and do not introduce additional service delivery priorities. Hence, the Council does not generally engage in wider consultation on enabling plans and strategies.

4.3 Capital Plan

Despite the uncertain economic climate Charnwood has an ambitious Capital Plan which runs through to March 2012 and reflects the strategic priorities of the Council. In particular, the plan envisages major expenditure in line with its Decent Homes strategy, significant investment in leisure projects including a £3.1m project to deliver the South Charnwood Leisure Centre and regeneration schemes for Loughborough Town Centre and Loughborough Eastern Gateway. In addition, external funding of over £800k was successfully bid for to redevelop Gorse Covert Community Centre in Loughborough and this has recently reopened.

The three year Capital Plan to the end of March 2012 has a gross spend of nearly £31.7m with £21.7m of external funding. The remaining £10m is being funded from capital receipts which the Council has either already received or expects to receive over the period to 31 March 2012. On present trends the availability of new capital receipts after March 2012 will be much lower and this will result in a reduced level of capital investment in the borough by the Council.

4.4 Council transformation

Charnwood is transforming itself as a Council through the outsourcing of functions to external service providers, sharing services with neighbouring local authorities and searching for other arrangements in order to underpin the Corporate Plan. The management of council houses has rested with Charnwood Neighbourhood Housing Ltd (CNH) since December 2007 and negotiations are taking place to outsource the provision of the Council's Housing Benefits and Council Tax collection services to a private sector provider. In staff terms, Charnwood's head count will reduce to 440 people from over 710 in 2007 before the transfer of staff to CNH.

This smaller organisation is designed to deliver operational improvements alongside cost savings; the financial management challenge will arise through the need to maintain financial flexibility within the reduced direct cost base.

5 The Financial Strategy

This Financial Strategy considers the financial outlook for the Council in the medium term and for the purposes of the financial projections we have concluded that the medium term constitutes the three financial years ending 31 March 2013. This period is not coterminous with the current Corporate Plan which runs through to 2012 but will be used in conjunction with that Plan to ensure that the Council's priorities are adequately funded to provide the level of service envisaged by that Plan.

This section focuses on the Council's 'General Fund', essentially all aspects of Council finances except for the ring fenced specific funding relating to the Housing Revenue Account (HRA). The HRA is considered in section 6.

This section considers in turn:

- Sources of finance
- Assumptions underpinning the three-year financial projections
- A summary of three-year financial projections
- The impact on service delivery

5.1 Sources of finance

In creating the Financial Strategy the following sources of funding for service delivery and service enhancements were considered:

- Council Tax precepts (including the Loughborough Special Rate)
- Government grant income
- Charging for services
- Use of existing financial resources ('balances') built up over time
- Prudential borrowing
- Investment income

These are considered in turn below.

5.1.1 Council Tax

There is understandable resistance from local citizens to any significant increases in Council Tax and the current administration is committed to restricting growth in the Charnwood Council Tax precept. Central Government is also very sensitive to significant increases in this tax and reserves the right to cap increases that it regards as 'excessive'. Whilst no firm 'capping' limit is set in advance by the Government any increase of 5.0% or more would be unlikely to escape capping.

In comparison to other Districts Charnwood Borough Council's Council Tax charges are amongst the lowest in the country as the data from the Department of Communities and Local Government below illustrates:

Table I: Comparison of District Band D Council Tax charges 2009/10

	District Council Tax Band D	Rank (of 201)		District Council Tax Band D	Rank (of 201)
National Picture			Leicestershire Authorities		
<u>Lowest</u>					
Breckland	£68	1	Hinckley & Bosworth	£110	10
West Oxfordshire	£79	2	Charnwood	£123	20
Hambleton	£87	3	Blaby	£135	42
Charnwood	£123	20	Harborough	£166	108
			Melton	£174	128
			North West Leicestershire	£180	141
			Oadby & Wigston	£199	168
<u>Median</u>			<i>Source - Department for Communities and Local Government * Calculation includes Band D and Share of Loughborough Special Rate (or Equivalent) spread across whole tax base</i>		
South Holland	£160	101			
North Devon	£161	102			
Gravesham	£162	103			
<u>Highest</u>					
Weymouth & Portland	£262	199			
Adur	£268	200			
Ipswich	£307	201			

Despite Charnwood's low tax base it is assumed that increases of only 2.75% will be levied in the next three years of the Financial Strategy.

The annual inflation rate over the past four years from 2006 to 2009 (Consumer Price Index (CPI) increases for twelve months to the end of June) have been 2.2%, 2.6%, 3.3% and 2.1%. Charnwood's Council Tax increases for the past four years have been 3.5%, 2.5%, 2.5% and 3.5%. The actual amount of Council Tax collected may also vary in line with the tax base, essentially the number of properties against which Council Tax is levied. However, this variation is considered unlikely to be significant during the life of the Financial Strategy.

5.1.2 Loughborough Special Rate

The town of Loughborough does not have the equivalent of a Town Council and the role that such an organisation would fulfill is undertaken by Charnwood Borough Council.

The Loughborough Special Rate is levied on residents of Loughborough by the Borough Council and is used for activities specifically related to Loughborough town. This set of activities is comparable to those performed by Towns and Parishes and used by other Councils in equivalent situations. These activities have been validated by the Council. Activities include maintenance of parks, cemeteries and memorials, management of allotments and costs associated with the Loughborough Fair and festive decorations. A full list of activities is set out in the Budget Book issued by the Council each year and available at:
<http://www.charnwood.gov.uk/pages/financialdocumentsforpublicuse>

Historically, the Loughborough Special Rate has been volatile reflecting the time lag between the expenditure outturns and determination of the rate. Changes in accounting processes and management of expenditure have reduced this volatility and for the purposes of future years' projections the Special Rate is assumed to increase in line with main Council Tax charge.

It should be noted that when the government calculates the level of increase, year on year, on Charnwood's Council Tax it includes both the main Borough charge and the Loughborough Special Rate.

5.1.3 Government grant income

The Council receives approximately two-thirds of its income through formula grants from Central Government, principally the centrally allocated share of National Non-Domestic Rates and the Rate Support Grant. The grants for financial years 2009/10 and 2010/11 were determined as part of the Comprehensive Spending Review of autumn 2007 (known as CSR07) and showed minimal inflationary growth.

In creating the Financial Strategy projections therefore, one of three years grant income is known. The final two years, 2011/12 and 2012/13, are due to be determined in the next Comprehensive Spending Review scheduled for autumn 2010 (CSR10). The condition of Central Government finances in autumn 2010 is anticipated to be still weak given the costs already incurred in supporting the banking sector, current tax and expenditure policies and the natural additional costs arising from increased benefit payments etc. Accordingly, no growth in formula grants for either 2011/12 or 2012/13 has been assumed.

Table 2: Formula grant income

	2010/11	2011/12	2012/13
	CSR 07	CSR 10	CSR 10
	Known	Estimate	Estimate
Formula Grant	12,513	12,513	12,513
Increase on Prior Year	1.8%	Nil	Nil

5.1.4 Charging for services

In common with other Authorities Charnwood makes a charge to users for certain services provided in areas such as leisure centre admissions, building control and car parking. Generally, due to the restrictions placed on Local Government organisations by regulation and the impact of the economic cycle it is not always easy to actively manage the income from service charges.

In Charnwood, charging structures tend to be developed within services on a service specific basis having regard to objectives such as recycling rates (which informs charges set for garden waste collection) and supporting local businesses (which informs car parking charges) as well as pure income generation.

The current reduction in the rate of Value Added Tax (VAT) finishes in December 2009 and as all income and expenditure is accounted for on a net basis, ie after VAT has been taken out, this will not have an effect on the Council's finances. There might be a slight impact on volumes as the full rate is recharged to end users but this will not have a material impact.

Generally, the Financial Strategy reflects the impact of the economic environment on income generation but does not seek to influence income generation activities.

5.1.5 Use of existing financial resources

Currently, Charnwood retains a number of 'balances' on its balance sheet, representing amounts that the Council may use to deliver or enhance Council services. Broadly, these are of three types:

- The General Fund balance that can be used to fund any type of expenditure
- Balances that may be used to fund any type of expenditure but which have been earmarked for specific uses by the Council, and
- Balances that are restricted in use by Government regulation that can be used to fund only specific types of expenditure, usually of a capital nature.

There are also other balances on the Council's balance sheet created as a result of Government regulation or accounting rules. These balances may not be used to fund expenditure of any type.

In recent years Charnwood has made substantial investments in service delivery but the availability of financial resources is now very limited and the Strategy therefore assumes that:

- The General Fund balance will be maintained at a level not less than a value of £1m in line with good practice (discussed in more detail at section 7);
- The Reinvestment Reserve (an earmarked reserve) will be maintained to enable investment in services and together with the Local Authority Business Growth Incentive (LABGI) Reserve will not reduce below a level of £500k. It

should be noted that there might be transfers between these reserves during the period covered by this Strategy,

- Other earmarked reserves –Performance Reward Grant Reserve and Capital Plan Reserve – will all be utilised during 2009/10 in line with the current budget.

5.1.6 Usable Capital Receipts Reserve

The Usable Capital Receipts Reserve represents the proceeds of asset sales available to meet future capital expenditure. The use of this reserve is restricted for application on items of a capital nature. Being less flexible than other reserves, Charnwood have a policy of applying the Usable Capital Receipts Reserve as first preference when financing capital schemes.

The historical proceeds of significant asset sales notably that of Maxwell Drive, created a healthy Usable Capital Receipts Reserve for the Council. Currently however, the prospects for capital receipts are weak; sales of Charnwood council houses to tenants have been significantly affected by the ‘credit crunch’ whilst the sale of land for housing or other development is restricted by the adverse economic conditions and financial weakness within the construction industry. In the year to 31 March 2009, there were no capital receipts (excluding council house sales) and there have been none so far in 2009/10. Accordingly, the level of Usable Capital Receipts is predicted to reduce by £7.3m over the three years of the strategy from its level of £8.1m at the end of March 2009. Please see the forecast balance sheets in Appendix 3.

Within Charnwood a well-established process exists for the management of the capital plan. For the purpose of the Financial Strategy we are therefore able to assume that sufficient resources exist, or will be generated, to finance all uncompleted schemes within the current Capital Plan. Funding required beyond this point will rely on the Council’s ability to generate new and significant capital receipts from asset sales (deemed unlikely given the economic outlook) or Prudential Borrowing, which is discussed further below.

5.1.7 Use of Prudential Borrowing

Charnwood has been able to avoid the use of borrowing in recent years. Whilst funds could be raised for investment purposes, the interest and principal payable on such loans would be a ‘revenue’ charge to the Council that would impinge upon funds available for day to day service delivery.

Other councils are now starting to make increasing use of Prudential Borrowing to finance their capital programmes as capital receipts have dried up. This option is a possibility for Charnwood but given the availability of internal sources of funding, and the additional pressure that borrowing would place on funds available for day to day service delivery, there are no general plans to engage in prudential borrowing in the medium term.

5.1.8 Use of Prudential Borrowing regarding the Decent Homes strategy

The Council does, however, plan to undertake substantial Prudential Borrowing in line with its 'Decent Homes' strategy. This strategy is dependent on the business plan for CNH which aims to achieve 'Two Star' status for its housing management service in early 2010. Achievement by CNH of Two Star status will then allow the Council to borrow the substantial amounts needed, currently estimated at £36m, to invest and achieve Decent Homes status for the stock. The financial arrangements are somewhat complex; whilst the loans will sit on the Charnwood General Fund balance sheet the actual management of spend will be undertaken by CNH. Under current regulations the Housing Revenue Account will reimburse the Charnwood General Fund over time and Charnwood itself will receive Government funding on an annual basis (known as 'Item 8 debit') to enable repayment of the loans.

However, as explained further in section 6, the whole funding regime for the HRA is currently under review and the mechanisms used in future may change.

5.1.9 Investment strategy

Charnwood Borough Council holds substantial short-term investments, principally cash deposited for short periods on money markets. In recent years these have had a value in the range of £20m - £30m at any point in time. Broadly, these amounts represent a combination of Council Reserves (such as funds earmarked to fund the Capital Plan) and Council Tax collected on behalf of the County Council, local police and fire authorities, and parishes. The investment income generated from these balances is an important source of funding for the Council.

The Council generated in excess of £1.7m in investment income in 2009/10 but, as mentioned earlier, the current interest rate outlook combined with reducing cash balances (as the capital plan is implemented) and the more restrictive investment policy in the light of current bank credit ratings will result in this level of income being much reduced over the three years of the Strategy.

Treasury management strategies and policies are discussed in detail at section 7.

5.2 Assumptions underpinning the three-year financial projections

The projections presented use the latest budget numbers available adjusted for known 'one-off' items of income and expenditure. These numbers are then projected across future years using a number of detailed assumptions around increases and decreases in the various types of income and expenditure. Certain key assumptions, those considered to be materially significant in the construction of the Financial Strategy, have been used to model different financial scenarios – the Pessimistic Case, the Central Case and the Optimistic Case. These key assumptions are discussed below.

5.2.1 Council Tax and Loughborough Special Rate increases

Council Tax rises are envisaged at 2.75% per annum in the three years of the Financial Strategy as described previously. The Loughborough Rate is expected to increase at the same rate over this period.

5.2.2 Inflation rates

Different inflation rates have been applied to varying types of income and expenditure with an overall rate of 2% being used. The principal cost type within the Council are those relating to staff. The models assume that salary inflation will mirror the strength of public finances and the wider economy and the Central Case reflects this with salary inflation restricted to 1% in 2010/11 and 1.5% in subsequent years of the Strategy.

5.2.3 Income

Three of the Council's major income streams - Development Control, Building Control and Land Charges - have shown sharp falls in response to deterioration in the wider economy. The Central Case assumes that the current weak demand for these services continues through 2010/11 and then very modest increases are forecast for 2011/12 and 2012/13.

5.2.4 Concessionary travel costs

The Council is required to operate a concessionary travel scheme. The bulk of costs incurred relate to free bus travel for the Over 60s and the reimbursement of bus operators. Central Government theoretically funds the costs of the scheme through a specific grant for concessionary travel and other monies embedded within the main formula grants. In practice this funding has fallen well short of scheme costs due to greater than expected uptake combined with the fuel costs passed on by bus Operators and systemic inequalities in the mechanics of the scheme.

The Central Case assumes total costs of the scheme will continue to increase by 2% per annum over the three years but that the funding from Central Government will be frozen after 2010/11. Therefore the current funding gap will widen.

There is a prospect that responsibility for running the travel scheme will be transferred to Leicestershire County Council from 2011/12. However, this has not yet been confirmed and the calculation of any transfer of funding is also not known. In view of this the Strategy assumes that any such transfer would have a neutral effect on the Council's finances.

5.2.5 Environmental Services and other contract costs

The Council's environmental services, fleet and recycle processing contracts have all been re-tendered in 2009. The strategy reflects the results of these new contracts which overall have a positive impact.

5.2.6 CNH Service Level Agreements (SLA)

CNH, the Council's housing management subsidiary, currently uses the Council to provide some of their support services. CNH is required to seek best value in procurement for all of its services and during 2009/10 they terminated some of the agreements for services. The Strategy assumes that the remaining services will continue to be provided in line with the current SLAs as no further termination notices have been received.

5.2.7 Outsourced and shared services

The Council remains committed to outsourcing its Revenues and Benefits services and detailed negotiations continue with a prospective service provider with a view to completing a deal in late 2009. The Council's target is to achieve savings of at least 10% over the life of the contract and the Central Case assumes that savings are achieved in line with projections included in the pricing schedule.

5.2.8 Interest rates

The outlook for interest rates is now more settled, but at a very low rate and our expectations are that interest rates will remain generally low across the period of the Financial Strategy but will vary in line with the outlook for economic growth and inflation at any particular point in time.

Views on interest rates from the Council's brokers are that the 0.5% base rate will continue for 2009/10 and then increase in steps to 2.5% by March 2011 and then to 3.5% in 2012 and 4.00% in 2013. For the purposes of the Central Case we assume that returns on our investments for 2010/11 will be 3.02%, rising to 3.68% in 2011/12 and 4.50% in 2012/13.

5.2.9 Capital charges

Capital charges are effectively the depreciation charged each year on fixed assets used by the Council to provide its services. In addition, they include any charges that cover the situation where the Council has used capital to provide an asset which it does not use in its own services, for example a capital grant to a parish. Under current regulations these charges are not taken into account when setting the Council Tax and are deducted from the Net Service Expenditure used in the Central and other cases.

5.2.10 Assumptions

Table 3: Summary of assumptions for Central Case

Summary of Assumptions - Central Case Figures that are not percentages are in £'000s	2010/11	2011/12	2012/13
Council Tax - % increase	2.75%	2.75%	2.75%
Loughborough Special Rate - % increase	2.75%	2.75%	2.75%
Inflation Rate Applied to Salaries - % increase	1.00%	1.50%	1.50%
Central Government Grants Increase %	1.80%	0.00%	0.00%
Development Control (income)	-908	-926	-944
Building Control (income)	-448	-456	-466
Land Charges (income)	-179	-182	-186
Concessionary Travel Costs	1,841	1,896	1,954
Environmental Services Contract Costs	4,063	4,185	4,312
Reduction in Environmental Services Income	244	244	240
Net Saving of Outsourcing of Services to Capita	-80	-82	-85
Increased Pension costs	219	334	339
Reduction in Insurance Costs	-100	-100	-100
Interest Rates - average for CBC - internal and external	3.02%	3.68%	4.50%

The assumptions for the Pessimistic and Optimistic Case scenarios together with the associated summaries of three-year financial projections are set out at Appendices 1 and 2 respectively.

5.3 Summary of three-year financial projections – Central Case

Set out below is the Central Case based on the assumptions outlined in the previous paragraphs:

Table 4: Financial Projection - Central Case

<u>Central Case - General Fund</u>	<u>2010/11</u> £000	<u>2011/12</u> £000	<u>2012/13</u> £000
Net service expenditure	24,276	24,757	25,297
Less: Capital charges	(3,566)	(3,566)	(3,566)
	<u>20,710</u>	<u>21,191</u>	<u>21,731</u>
Interest payable	237	237	237
Interest (receivable)	(690)	(790)	(1,265)
	<u>20,257</u>	<u>20,638</u>	<u>20,703</u>
Contribution to Capital Programmes	170	170	170
Total net expenditure	<u>20,427</u>	<u>20,808</u>	<u>20,873</u>
Financing strategy			
Council Tax	(5,520)	(5,672)	(5,828)
Loughborough Special Rate	(1,222)	(1,255)	(1,290)
Formula grants	(12,513)	(12,513)	(12,513)
Concessionary travel grant	(372)	(372)	(372)
Total income	<u>(19,627)</u>	<u>(19,812)</u>	<u>(20,002)</u>
Total net expenditure (from above)	<u>20,427</u>	<u>20,808</u>	<u>20,873</u>
Funding shortfall	801	996	871
Financed by:			
Planned use of balances	(67)	0	
Deficit on collection fund	49	50	50
Change to use of balances	(783)	(1,046)	(921)
Other (savings required)/funding balance	(0)	0	(0)
	<u>(1)</u>	<u>1</u>	<u>(1)</u>

Summary balance sheets reflecting the above case and the effect on balances shown below are included in Appendix 3. Whilst the Council does not use its balance sheet to support credit ratings or seek finance they are an important document and are included for completeness. It should be noted that the balance sheets and the revenue information are all presented in line with the current accounting regime under which the Council operates rather than the forthcoming International Financial Reporting Standards.

<u>Revenue Balances</u>	2010/11	2011/12	2012/13
	£000	£000	£000
Balances brought forward	4,515	3,665	2,619
Net use of balances as above	(850)	(1,046)	(921)
Balances carried forward	3,665	2,619	1,698
Working Balances	3,034	1,988	1,067
Reinvestment Reserve	268	268	268
LABGI	363	363	363
	3,665	2,619	1,698

5.4 Financial Strategy Central Case financial projection – comments and implications

The main implications of the Central Case projection are that:

- Whilst the projections show that the shortfalls could be funded from reserves for the three years, this is not a sustainable solution as reserves would drop below the minimum level of £1.5m in 2013/14.
- Structural alteration to the Council's cost base is needed of approximately £950k per annum
- This imbalance of £950k between revenue and expenditure must be resolved by reducing expenditure by £950k per annum as there is not the potential to increase income by this amount. Whilst there may be increases in income in the future they will not be sufficient to cover this shortfall.
- The Central Case projections essentially assume an extended period of weak economic activity but no further significant deterioration in economic outlook.

Pessimistic and Optimistic Cases are presented in the appendices to this document.

6 The Housing Revenue Account

The Housing Revenue Account (or HRA) is a 'ring fenced' set of transactions that sit within the wider financial records of the Council. The principal components of the Charnwood Borough Council HRA are:

Income

- Rental income from council housing £17.3m
- Other rents (shops, land and garages) £0.3m
- Service charges of various descriptions £1.1m
- 'Major Repairs Allowance' – for capital expenditure £3.7m

Expenditure

- Supervision and management (including allocations) £1.1m
- Depreciation on housing stock £4.1m
- CNH management fee £9.1m
- 'Negative Housing Subsidy' – payable to Government £7.8m

There is a surplus or deficit on the HRA each year which is added to the brought forward HRA balance. This balance should always be in surplus but at 31 March 2009 it was only £19k against a target balance of £644k. It is unlawful for the HRA to fall into deficit and the implications of this for the Council's Decent Homes strategy would be grave. Rebuilding this balance is therefore a priority; however, the nature of the HRA means that the Council has very limited options in doing this.

Rent increases are constrained by Central Government whilst the Negative Housing Subsidy is also calculated by, and payable to, Central Government. The calculation of this is complex and consultation is currently underway to scrap the way Housing Revenue Accounts operate and especially the subsidy system. Effectively councils either receive a subsidy based on their calculated 'needs' or, as in Charnwood's case, they pay a negative subsidy to the government which is redistributed to the 'needy' councils.

Under the proposed measures the government would still control rents but councils would retain all their rental income and could spend it as they see fit, though it would still have to be spent on housing and not become a contribution to the General Fund. However, the government has a notional debt of £17bn in relation to housing and it wants to reallocate this in some form or other as part of this loosening of the subsidy regime. At present it is not possible to calculate the precise effect of this on Charnwood as there are various options being considered and the model for reallocation affects all the Councils involved and is not transparent. Therefore it is not possible to accurately plan for this potential change at the moment.

In view of this, and bearing in mind that it is not allowable for the HRA to receive funding from the General Fund, the main avenue to rebuild the HRA balance is through a reduction in the level of the CNH management fee. This fee has been

reduced for 2009/10 and is expected to remain restricted for at least two more years. In addition, attention is focused on reducing the level of rents lost through properties being empty. This focus will aim to reduce the average time that each property is empty so that the amount of rent lost is minimised.

This strategy for addressing the very low level of HRA balance is not undertaken lightly and it is understood that CNH's ability to achieve its business plan, and in particular 'Two Star' status for its housing management service in early 2010 (a key component of the Council's Decent Homes strategy), may be compromised. CNH also has to focus on its own activities to ensure that losses do not continue and that the deficit in its first 16 months of activity is reversed over a reasonable time period.

The Council is working closely with CNH to mitigate the impact of required restrictions on the level of the management fee.

7 Principal financial policies and processes

7.1 General

The Council at all times seeks to comply with relevant guidelines and regulations and strive for best practice in managing its accounting processes and presenting its statement of accounts. In particular the Council recognises the importance of proper administration of its financial affairs as required by Section 151 of the Local Government Act 1972, the requirement to set a balanced budget on an annual basis and the requirement to present fairly the Council's statement of accounts in line with the CIPFA Code of Practice on Local Authority Accounting. The Council received an unqualified audit report for its accounts for the year ended 31 March 2009.

7.1.1 Annual budget

Charnwood sets a balanced budget on an annual basis as required by legislation. Budgetary control is obtained through the detailed compilations of budgets within closely specified parameters; once approved, the detailed budgets confirm Council's authority for Directors to incur such expenditure on behalf of Council.

Historically, the Council has used incremental budgeting, which is the most widespread technique in use. In incremental budgeting amounts are added each year for inflation, where applicable, or additional service growth. This is generally the lowest cost method in terms of budgetary processes but can be argued to lack appropriate challenge of the base position. Other budgetary processes, such as priority based budgeting, are more time consuming but do offer a structured opportunity to challenge the base position. A prioritisation exercise is currently underway which will be in effect a half way house between full priority based budgets and the current process and is expected to provide broad guidelines for the Council's preferred spending options in 2010/11 onwards.

7.1.2 Revenue budget monitoring targets

The Council recognises the importance of avoiding material over or under spending against the revenue budget. It is widely understood that over spending against budgets is unacceptable; however, material under spending should also be avoided as it implies that services that could have been provided to citizens have not been delivered. Clearly, there are always specific circumstances within individual services that result in legitimate over or under spending but overall the actual outturn expenditure should correlate closely to that budgeted.

Charnwood therefore has a target that the revenue outturn will be within 2% of the controllable service expenditure budget. This is in line with generally accepted good practice.

7.1.3 Virement and Carry Forward policies

The Financial Regulations and Financial Procedures of the Council set out the parameters within which money may be reallocated, or 'vired', between budget headings. These limits are reviewed periodically to ensure an appropriate balance between flexibility and control. Virement between Directorates is much more restricted than virements within Directorates whilst money may not be vired from capital to revenue expenditure budgets.

The 'carry forward' of budgets underspent into subsequent years is generally discouraged. Budgets are only carried forward on an exceptional basis and are approved by Cabinet as part of the year end financial reporting process.

7.1.4 Contingencies and use of reserves

The Council should maintain a prudent approach to service planning and seek to avoid the use of reserves (or 'balances') to fund recurring revenue expenditure. In principle the Council has operated this policy but in practice recent years have seen a growth in the cost base that has not been reflected in equivalent increases in revenue.

As mentioned above, whilst balances could be used for the next three years this is not sustainable and Service planning will need to reflect this.

The Council does maintain a small contingency fund within the overall revenue budget reflecting financial risks identified during the service planning process.

7.1.5 Balance of reserves

The Council strives to maintain minimal balances on certain reserves to ensure that material financial shocks, such as might arise from some emergency scenario, can be absorbed by the organisation. The objective of these balances is to ensure that no Council service would have to be reduced due to the occurrence of an event that requires an immediate resource.

The reserves in question are the General Fund and the Housing Revenue Account balance which relate to general Council services and housing services respectively. There are alternative good practice suggestions around the level at which the General Fund balance should be maintained. Examples of these suggest a level equating to between 1% and 5% of Gross Revenue expenditure or around 5% of Net Revenue expenditure. For Charnwood this would represent a balance of between £0.7m and £3.5m and informs the Council's policy of maintaining a minimum General Fund balance of £1m.

There are less good practice alternatives around the level at which the Housing Revenue Account be maintained. Precedence suggests that the HRA balance be maintained at a level equivalent to £110 per council dwelling. This would represent a balance on the Housing Revenue Account of £644k against that of £19k existing at

31 March 2009. This position must be reversed and close monitoring and rebuilding of this reserve up to desirable levels are an ongoing financial priority for the Council. The strategy for achieving this was discussed in section 6, and whilst rebuilding the HRA balance is a difficult task target balances for the HRA are set at:

- 31 March 2010 £0.23m
- 31 March 2011 £0.38m
- 31 March 2012 £0.55m
- 31 March 2013 £0.65m

7.1.6 Treasury management

It is public knowledge that the Council has £1m deposited with Heritable Bank, the UK subsidiary of the failed Icelandic Bank Landsbanki. At this time it is anticipated that approximately 80% of this investment will be recovered and £167k was received in July 2009 and a further payment is expected in December 2009.

Having experienced this bank failure it is tempting to place very tight restrictions on the Council's lending. However, it is worth noting that investment income is an important source of funding for the Council and restricting investment opportunities has significant financial consequences. To put this into context, the safest home for the Council's investments is the HM Treasury backed Debt Management Office (DMO). However, the returns on investments in the DMO are very low for short term debt as they do not have a great demand for very short term funds. Therefore, the Council must ensure that it achieves a reasonable rate of return whilst protecting its investments.

Revised treasury management operating guidelines combined with an updated treasury management strategy were approved in February 2009 and these allow the Council's finance staff appropriate levels of latitude in the day to day management of treasury operations though the investment strategy is weighed towards protection of capital and will probably remain so until the financial climate has improved.

8 Value for Money and efficiency savings

A Value for Money (VFM) exercise across the organization is underway and various services are being reviewed in addition to those already identified for outsourcing.

Our view of VFM is as follows:

- We (the Council) needs to ask ourselves whether we are doing the right things, whether we are doing the right things well and whether we could do things better
- Doing the right things means demonstrating a clear link between resident consultation, priority setting, allocation of resources, efficient use of resources and effective outcomes
- Evidenced through an embedded benchmarking process and positive scores related to VFM in the new Audit Commission inspection regime (within the new Comprehensive Area Assessment) the Council will know that it is doing things well.

The Financial Strategy projections are quite clear in their implication; the Council needs to make significant savings against the current cost base. The principal external measure of efficiency now used is National Indicator (NI) 179 which requires the Council to make year on year efficiency savings of 3% which should be 'cashable' but which should not compromise service delivery. This NI179 target is extremely challenging given these conditions.

In implementing any cost reduction measures the Council will always strive to minimise the impact on service delivery to its residents.

9 Working with partners

Working with partners of various types is an increasingly important theme across Local Government. Charnwood has a tradition of providing grants to various community groups which will be continued. However, we now seek to manage our relationships with these partner organisations more actively. In particular we seek to ensure:

- Grant monies will be disbursed to support explicit objectives of the Council
- Service level agreements with partner organisations are developed to allow the Council to monitor the delivery of outputs and demonstrate the achievement of the Council's objectives through partnership working.

9.1 Leicestershire Together

Leicestershire Together describes itself as the 'partnership of partnerships for Leicestershire'. Charnwood Borough Council is committed to playing its part in the development of this partnership group.

The Leicestershire Performance Framework (LPF) sets out the objectives of Leicestershire Together. Key LPF objectives towards which we direct significant financial resources include (references are those from the LPF):

- 3.7: The housing needs of the people of Leicestershire are met
- 3.8: New developments are built to higher design, security and environmental standards
- 4.3: Less waste is produced and a reduced proportion of this goes to Landfill
- 6.1: Improved physical health, well-being and community cohesion through enhanced access to sport, recreation and cultural activities

10 Risk assessment and mitigation

10.1 Policies and procedures

Charnwood actively manages and reviews its finances on an ongoing basis through the regular monthly process of monitoring revenue budgets. Risks are also formally assessed and recorded as part of the annual update of the Financial Strategy and at the setting of the full-year budgets. In addition, Capital Expenditure is monitored periodically and reports made to the senior Management Team, Cabinet and Performance Scrutiny Committee.

Assessing risks on a regular basis allows these to be mitigated through the financial planning and budgeting processes.

10.2 Risks identified

The principal financial risks identified in the construction of the Strategy are as follows. The potential impact is assessed against the Central Case Financial Strategy projections:

Table 5: Summary of principal financial risks identified

	Quantum of Income/Spend	Risk Assessed	Potential Annual Impact
Income Streams	£1.5m	+/- 20%	+/- £0.30m
Concessionary Travel	£1.8m	+/- 15%	+/- £0.27m
Staff Pay Award	£13m	+ 1%	+£0.13m
Interest Rates	£0.9m	+/- 20%	+/- £0.18m

Appendix I - Financial Strategy Projection – Pessimistic Case

Compared to the Central Case the Pessimistic Case assumes an even less benign general economic situation and more downside events specific to Charnwood's own position. Except for the assumptions below, all other assumptions follow the Central Case:

- Inflation at 3.0% per annum rather than 2.0%
- Salary increases 0.5% higher than the Central Case
- Concessionary travel costs rising at 4% rather than 2%
- Development Control, Building Control and Land Charges income running at £108k below the Central Case per annum.
- Council Tax rising by 2.5% in the last two years rather than 2.75%
- Pension costs being 1% higher per annum from 2011/12.
- The Central Government grant being cut by 2% per annum in both 2011/12 and 2012/13.

Table A1.1: Pessimistic Case

<u>Pessimistic Case - General Fund</u>	<u>2010/11</u> £000	<u>2011/12</u> £000	<u>2012/13</u> £000
Net service expenditure	24,731	25,388	26,082
Less: Capital charges	(3,566)	(3,566)	(3,566)
	<u>21,165</u>	<u>21,822</u>	<u>22,516</u>
Interest payable	237	237	237
Interest (receivable)	(684)	(790)	(1,265)
	<u>20,718</u>	<u>21,269</u>	<u>21,488</u>
Contribution to Capital Programmes	170	170	170
Total net expenditure	<u>20,888</u>	<u>21,439</u>	<u>21,658</u>
Financing strategy			
Council Tax	(5,520)	(5,658)	(5,799)
Loughborough Special Rate	(1,222)	(1,255)	(1,290)
Formula grants	(12,513)	(12,263)	(12,017)
Concessionary travel grant	(372)	(365)	(357)
Total income	(19,627)	(19,541)	(19,464)
Total net expenditure (from above)	20,888	21,439	21,658
Funding shortfall	1,262	1,899	2,194
Financed by:			
Planned use of balances	(67)	0	0
Deficit on collection fund	49	50	50
Change to use of balances	(1,244)	(1,704)	0
Other savings required	(0)	(245)	(2,244)
	<u>(1)</u>	<u>0</u>	<u>0</u>

<u>Revenue Balances</u>	2010/11	2011/12	2012/13
	£000	£000	£000
Balances brought forward	4,515	3,204	1,500
Net use of balances as above	(1,311)	(1,704)	0
Balances carried forward	3,204	1,500	1,500
Working Balances	2,573	869	869
Reinvestment Reserve	268	268	268
LABGI	363	363	363
	3,204	1,500	1,500

The main implications of the Pessimistic Case projection are that:

- Balances could only cover the situation until part way through 2011/12.
- Structural alteration to the Council's cost base would be needed of approximately £2.3m per annum

Appendix 2 - Financial Strategy Projection – Optimistic Case

Compared to the Central Case the Optimistic Case assumes an more benign general economic situation and less downside events specific to Charnwood's own position. Except for the assumptions below, all other assumptions follow the Central Case:

- Inflation at 1.0% per annum rather than 2.0%
- Development Control, Building Control and Land Charges income running at £49k above the Central Case per annum.
- Council Tax rising by 3.0% in the last two years rather than 2.75%
- Pension costs being 1% higher per annum from 2011/12.
- The Central Government grant increasing by 1% per annum in both 2011/12 and 2012/13.

<u>Optimistic Case - General Fund</u>	<u>2010/11 £000</u>	<u>2011/12 £000</u>	<u>2012/13 £000</u>
Net service expenditure	24,192	24,602	25,090
Less: Capital charges	(3,566)	(3,566)	(3,566)
	<u>20,626</u>	<u>21,036</u>	<u>21,524</u>
Interest payable	237	237	237
Interest (receivable)	(690)	(790)	(1,265)
	<u>20,173</u>	<u>20,483</u>	<u>20,496</u>
Contribution to Capital Programmes	170	170	170
Total net expenditure	<u>20,343</u>	<u>20,653</u>	<u>20,666</u>
Financing strategy			
Council Tax	(5,520)	(5,686)	(5,856)
Loughborough Special Rate	(1,222)	(1,255)	(1,290)
Formula grants	(12,513)	(12,638)	(12,765)
Concessionary travel grant	(372)	(376)	(379)
Total income	(19,627)	(19,955)	(20,290)
Total net expenditure (from above)	20,343	20,653	20,666
Funding shortfall	717	698	376
Financed by:			
Planned use of balances	(67)	0	
Deficit on collection fund	49	50	50
Change to use of balances	(699)	(748)	(426)
Other (savings required)	(0)	0	0
	<u>(1)</u>	<u>1</u>	<u>1</u>

<u>Revenue Balances</u>	2010/11	2011/12	2012/13
	£000	£000	£000
Balances brought forward	4,515	3,749	3,001
Net use of balances as above	(766)	(748)	(426)
Balances carried forward	3,749	3,001	2,575
Working Balances	3,118	2,370	1,944
Reinvestment Reserve	268	268	268
LABGI	363	363	363
	3,749	3,001	2,575

The main implications of the Optimistic Case projection are that:

- Balances could cover the situation all the way through the three years.
- Structural alteration to the Council's cost base would still be needed of approximately £650k per annum

Appendix 3 – Forecast Balance Sheets for the Central Case

	As at 31/3/2011 £'000	As at 31/3/2012 £'000	As at 31/3/2013 £'000
Fixed Assets	350,193	348,693	347,193
Long-term Debtors	40	40	40
Current Assets	31,119	31,119	31,119
Total Assets	381,352	379,852	378,352
Current Liabilities	(11,037)	(11,037)	(11,037)
Total Assets less Current Liabilities	370,315	368,815	367,315
Long-Term Assets/Liabilities	(31,329)	(30,736)	(30,191)
Total Assets less Liabilities	338,986	338,079	337,124
Financed by:			
Specific Accounts	(350,081)	(350,943)	(351,288)
Specific Reserves	17,450	17,450	17,450
Useable Capital Receipts	(2,329)	(1,367)	(823)
Earmarked Reserves	(631)	(631)	(631)
Fund Balances:			
General Fund Balance	(3,064)	(2,088)	(1,232)
HRA Fund Balance	(380)	(550)	(650)
Collection Fund Balance	49	50	50
Total Net Worth	(338,986)	(338,079)	(337,124)

The balance sheets above have been drawn up to reflect the effects of the Central Case. There is a fall in the value of Fixed Assets as Capital Expenditure is expected to decline and many of the larger schemes will not produce assets that will be directly used by the Council in the future, for example improving Loughborough Town Centre.

There are not expected to be any major changes to the Council's current assets or liabilities over the period.

On the lower section, Useable Capital Receipts are expected to decline due to the low level of sales and the use of the current receipts to fund the Capital Plan over these three years.

The decline over the three years of the council's Net Worth by £1.8m is less than 1% of the Balance sheet value and is not regarded as a significant risk to the Council.

Appendix 4 - Links to further information

The latest edition of the Council's financial statements and Budget Book can be found at:

<http://www.charnwood.gov.uk/pages/financialdocumentsforpublicuse>

The current version of the Council's capital plan can be found at:

http://www.charnwood.gov.uk/files/papers/cab_06_august_2009_item_10_capital_plan_amendment_report/Cab%2006%20August%202009%20Item%2010%20Capital%20Plan%20Amendment%20Report.pdf