



**SOUTHAMPTON CITY COUNCIL
MEDIUM TERM FINANCIAL STRATEGY
2015/16 TO 2019/20**

FEBRUARY 2016

MEDIUM TERM FINANCIAL STRATEGY 2015/16 to 2020/21

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1 **INTRODUCTION**

1.1 **Aims and Purpose of the Medium Term Financial Strategy**

The Medium Term Financial Strategy (MTFS) is a core part of the Council's strategic framework and plays a pivotal role in translating the Council's strategic plans and ambitions into action.

The MTFS focuses on determining the financial position for the next five years and takes into account major issues affecting the Council's finances, including international, national and regional economic influences as well as local factors and priorities.

This forecast forms part of the base assumptions for developing the overall budget, together with unavoidable service pressures agreed by the Cabinet and the Council's Management Team (CMT) that need to be taken into account in the overall budget deliberations.

The Council's Medium Term Financial Strategy has been developed in order to secure a forward looking approach and long term sustainability in service provision. The strategy concentrates on the principles that will provide a strong direction for the medium term.

An overarching MTFS is not only good practice, but is required to provide the strategic financial framework for the authority at a time of considerable pressure and change, be this delivering key priorities and ongoing efficiency gains, closer budget scrutiny, the management of financial pressures, or political change.

The key overriding aim of the MTFS is therefore:

'To provide a financial framework within which financial stability can be achieved and sustained in the medium term to deliver the Council's key strategic outcomes, priorities and sustainable services.'

In addition to its 6 key objectives of the MTFS are to:

- Provide the parameters within which budget and service planning should take place;
- Ensure that the Council sets a balanced and sustainable budget;
- Focus and re-focus the allocation of resources so that, over time, priority areas receive additional resources;
- Ensure that the Council manages and monitors its financial resources effectively so that spending commitments do not exceed resources available in each service area;
- Plan the level of local taxation in line with levels that the Council regard as being necessary, acceptable and affordable to meet the Council's aims, objectives, policies and priorities;
- Ensure that the Council's long term financial health and viability remain sound.

The MTFS therefore aims to move the Council on from the historical position of setting annual budgets in isolation to future years, to integrated service and financial planning over the medium term.

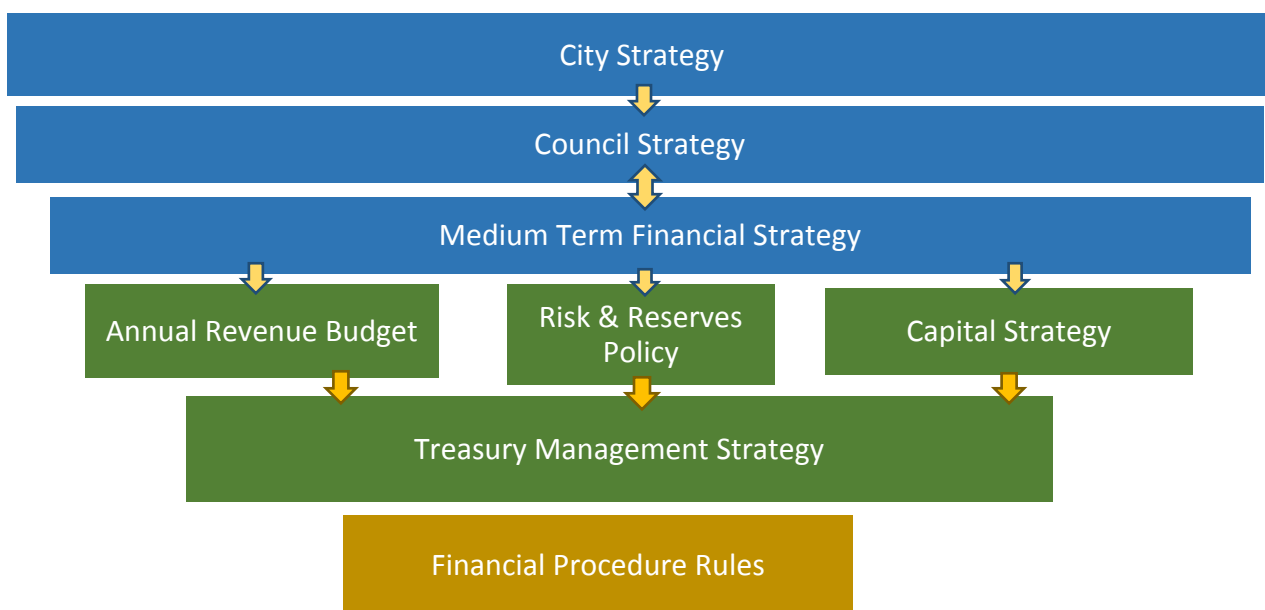
The MTFS recognises the key role that financial resources play in the future delivery of services, and enabling the effective planning, management and delivery of those services. A sustainable MTFS is therefore key to the effective delivery of the Council's overall aims of achieving better outcomes for residents.

The resulting Medium Term Financial Model does not however represent a committed budget, but provides the framework within which decisions relating to future service provision can be made. The detailed budget, taking account of constantly changing circumstances, will continue to be

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considered by the Council on an annual basis.

To aid understanding the diagram below sets out where the MTFs sits in relation to the City and Council Strategies and other financial strategies and plans.



1.2 **Key Influencing Strategies And Plans**

There are a number of strategies, policies and plans which impact on the direction of the Council and the day to day operations therefore impacting on the MTFs. The main items are detailed below along with the elements which impact on the MTFs.

1.2.1 **Southampton City Strategy 2015-25**

The MTFs is framed by the City Strategy 2015-2025, and the City Vision, which has been developed by Southampton Connect, a partnership group consisting of representatives from business, the public, voluntary and education sectors and the City Council.

The city vision is 'Southampton – City of opportunity where everyone thrives'. "This goal is to achieve prosperity for all. We want to build on Southampton's unique sea city location with exceptional transport links, its strong position nationally for economic growth, excellent reputation for teaching and learning, strong business community, good regional specialist hospital, varied retail offer, night time economy, vibrant voluntary and student communities, and rich diversity and cultural mix".

The City Strategy identifies three key priorities:

- Economic Growth with social responsibility
- Skills and Employment
- Healthier and safer communities.

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It also includes 4 cross cutting themes:

- Fostering City Pride and Community capacity
- Delivering whole place thinking and innovation
- Improving mental health
- Tackling poverty and inequality

Southampton Connect works closely with the key city partnerships to deliver against the vision, priorities and themes: Employment, Skills and Learning Partnership, Health and Wellbeing Board and Safe City Partnership.

1.2.2 **Southampton City Council Strategy 2014-17**

The City Strategy is a long term document, setting out priorities and themes which all partners will work together to achieve. Southampton City Council has a key role to play in this. The Council has set out its priorities in the Council Strategy 2014-17 which is due to be refreshed later this year.

The Council has agreed 7 main priorities within the Council Strategy. These are:

- Jobs for Local People
- Prevention and Early Intervention
- Protecting Vulnerable People
- Good Quality and Affordable Housing
- Services for all
- City Pride
- A Sustainable Council

We expect the shape of the Council, including the types of services we deliver and how we will deliver them, will be very different by 2017. The Council Strategy sets out that by 2017 we expect changes in terms of:

- Commissioning Services
- Community Ownership
- Better Customer Experiences
- More flexible ways of working
- A wide range of service delivery models
- Listen and improve learning from our mistakes
- Increased focus on digital capabilities of customers

A public consultation on priority outcomes was undertaken in August 2015 and the feedback received led to a focus on three major outcomes:

- Children and young people getting a good start in life;
- A modern, vibrant city where everyone works together to keep it clean and attractive; and
- Strong, sustainable economic growth.

This work is ongoing and as a result the Council Strategy will be updated later in 2016 to reflect the final conclusions of the review.

1.2.3 **Other Major Strategies and Policies**

As well as the overarching City Strategy and the Southampton City Council Strategy, there are a range of other strategies and policies and work programmes which will influence the MTFS.

The two other key financial strategies are detailed below:

1.2.3.1 **Capital Strategy**

The Council has a separate Capital Strategy that details the priorities of the Council in terms of capital expenditure and provides a framework for the Council's capital plans to be delivered within.

The Capital Strategy forms an appendix to the General Fund Capital Programme 2015/16 to 2019/20. The programme is approved each year in February by Council. Key issues and developments that are now incorporated in the strategy include:

- Recognition of the Council's Devolution proposals, noting that one of the key themes is accelerated housing delivery;
- Changes to the use of capital receipts, giving rise to the need to consider the use of this key funding source;
- Reviewing the alternative options for the disposal or development of land notably the setting up of a Development Company and the use of our property partner PSP;
- Recognition of the importance of the need for additional preventative Flood Defence schemes in the City;
- An update on the Council's Efficiency Strategy and transformation programme;
- The intention to set up a Property Investment Fund; and
- Clearer links to the service priorities.

1.2.3.2 **Treasury Management Strategy 2016/17 to 2018/19**

The Treasury Management Strategy is reviewed annually and provides the framework within which authority is delegated to the Service Director for Finance and Commercialisation to make decisions on the management of the City Council's debt and investment of surplus funds.

The City Council is able to borrow on a long term basis to finance capital and on a short term basis to manage cash flow fluctuations. The Council is also able to invest surplus funds.

The core elements of the 2016/17 strategy are :

- To continue to make use of short term variable rate debt to take advantage of the current market conditions of low interest rates;
- To constantly review longer term forecasts and to lock in to longer term rates through a variety of instruments, as appropriate during the year, in order to provide a balanced portfolio against interest rate risk;
- To secure the best short term rates for borrowing and investments consistent with maintaining flexibility and liquidity within the portfolio;
- To invest surplus funds prudently, the Council's priorities being:
 - Security of invested capital
 - Liquidity of invested capital

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- An optimum yield which is commensurate with security and liquidity; and

To approve borrowing limits that provide for debt restructuring opportunities and pursue debt restructuring where appropriate and within the Council's risk boundaries.

Investment Strategy

The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's investment balance has ranged between £92M and £125M. As at December 2015, the authority had internal investments amounting to £94.7M with an average rate of return of 1.30%.

The current strategy is to continue to diversify into more secure and/or higher yielding asset classes in 2016/17 as there is increasing risk and low returns from short term unsecured bank investments.

Investment limits are set as part of the strategy to help mitigate and spread risk across a number of financial institutions. The Service Director for Finance and Commercialisation has delegated authority to review these in year and they will be updated quarterly as relevant in line with advice received from the Council's treasury management advisors, Arlingclose.

Borrowing Strategy

As at the 31 December 2015, the Council's overall outstanding long term borrowing was £244M, at an average rate of 3.33% and an average maturity of 23 years. This has fallen by £9M since 1 April 2015 due to maturing debt which has not yet been replaced. The total long term debt portfolio is made up of loans from the Public Works Loan Board (PWLB) of £235M and market loans of £9M.

The Council's primary focus when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the Authority's long-term plans change is secondary to this. This is key to managing borrowing costs within the overall financial constraints of the authority.

By doing this the Council is able to reduce net borrowing costs and reduce overall treasury risk. Details of borrowing options are included in full within the Prudential Limits and Treasury Management Strategy 2016/17 to 2018/19.

The budget for debt interest paid in 2016/17 is £14.5M based on an average debt portfolio of £401.5M at an average interest rate of 3.6%. Investment income for 2016/17 is budgeted at £0.8M based on an average portfolio of £55M at an average of 1.44%. If actual levels of investments and borrowing, and actual interest rates differ from those forecast, performance against budget will be correspondently different.

1.2.3.3 Other Strategies

Below is a sample of further strategies that have been considered in drawing up the MTFs:

- Solent Economic Plan 2014-20
- Health and Wellbeing Strategy
- Better Care Plan
- Safe City Strategy
- Local Transport Plan and Transport Asset Management Plan
- Customer Strategy

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- Housing Revenue Account Business Plan 2016/17 to 2045/46
- Corporate Property Strategy and Asset Management Plan

1.3 **National and External Factors**

The MTFFS is set within the context of national economic and public expenditure plans, and takes into account the national legislation setting out the City Council's ability to borrow and to raise income from council tax and other sources.

1.3.1 **Comprehensive Spending Review 2015 (Autumn Spending Review)**

The Autumn Spending Review brought the announcement that the Government's intention was to radically change the way local authorities are funded by moving from 50% to 100% business rate retention and phasing out the Revenue Support Grant by 2020. Alongside this there would be additional responsibilities for local government to ensure the move was fiscally neutral to Central Government plans.

The Government also reiterated its earlier proposal, made in October 2015, to abolish Uniform Business Rates by 2020, giving local authorities the power to cut rates to boost growth, and giving directly elected mayors for combined authorities the power to levy a business rates premium for local infrastructure projects with the support of local business.

The current system of top ups and tariffs for redistributing revenues between local authorities will be retained.

The announcement also included a new flexibility allowing local authorities to spend up to 100% of their fixed asset receipts (excluding Right to Buy receipts) on the revenue costs of reform projects. Instead of holding assets that could be made surplus, councils will be able to sell them and reinvest in their services.

In recognition of the increasing demand for local authority adult social care services, councils will be able to levy a "social care precept" of up to 2% in council tax which must be spent exclusively on social care, with the potential to bring almost £2B more into the care system across the country. An announcement was also made that the Better Care Fund would be increased to support this and local authorities will be able to access an additional £1.5B by 2019-20.

Alongside savings in the Public Health grant, the Government announced it will consult on transferring new powers and the responsibility for its funding and elements of the administration, to local authorities.

The government will also consult on reforms to the New Homes Bonus, including means of sharpening the incentive to reward communities for additional homes and reducing the length of payments from 6 years to 4 years. This will include a preferred option for savings of at least £800M, which can be used for social care.

The national housing budget will be doubled, to £2Bn, and 400,000 affordable homes will be built, both to rent and to buy; almost half of these will be starter homes, while 135,000 will be available for the Help to Buy: Shared Ownership scheme.

Funding for the Troubled Families programme will continue, with efficiencies found from central budgets and current levels of funding will be maintained for community integration programmes, which will be targeted at supporting the recommendations made in Louise Casey's review of opportunity and integration in isolated and deprived communities.

The Chancellor confirmed that there will be 30 hours of free, funded early education for three and four year olds from 2017, for families working for more than 16 hours and whose incomes are below

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£100,000 per parent. Free childcare for the most disadvantaged two year olds will be maintained and funding for the sector will be increased by £300M to support more free places.

Funding for Free School Meals will be maintained, rates for the pupil premium will be protected and there will be an increase in the cash for the Dedicated Schools Grant.

The Government has expressed the view that local authorities will no longer run local schools, creating a governmental saving of £600m, on the Education Services Grant.

The government will phase out current school funding regime and create a new national funding formula to address the current inequities in funding, especially for the most disadvantaged pupils. Consultation for this will begin in the New Year, with a view to introducing the formula in 2017.

The Government reiterated its commitment to creating three million apprenticeships by 2020. It will also introduce an Apprenticeship Levy from 2017, set at 0.5% of employers' pay bill, in order to raise £3B a year.

Further information on the announcements contained within the Autumn Spending Review can be found at Appendix 3.

Devolution – Hampshire and Isle of Wight

The Council is currently an active partner in the Hampshire and Isle of Wight Devolution Deal, along with 15 other councils, two Local Enterprise Partnerships and two national park authorities, to Central Government to have more powers devolved to the area.

The Deal includes a proposal to retain 100% of the business rates collected within the area, currently 50% of all business rates collected are passed over to Central Government. In return for foregoing Revenue Support Grants from Central Government, the prospectus asks to keep 100% of business rates generated in the area and assumes the proposal will be fiscally neutral to the Government.

The proposals focus around four key themes: boosting business and skills for work; accelerating housing delivery; investing in infrastructure; and transforming public services.

Plans for homes include delivery of 10,000 homes over the next 10 years including in the priority home categories of rural affordable, low-cost starter, council new-build and extra care, by making use of exception sites including redundant public land. A commitment has been made to develop at least 2,000 new starter homes within the city. This has been supported to date by additional government funding with the introduction of Help to Buy in 2013.

Help to Buy was created to ensure that working people who were doing the right thing and saving for a deposit could achieve their aspiration of buying their own home through Government support. Home ownership is a key part of the government's long term plan to provide economic security for working people across the UK. To date this has been facilitated through Equity Loans and Mortgage Guarantee Schemes with 80% of completions to date being made by first time buyers with just under 50% of the properties being new build. The government announced two further initiatives in the Comprehensive Spending Review on 25th November 2015 which will further encourage this agenda.

- a) Help to Buy ISA introduced from 1st December 2015 whereby under the scheme, first-time buyers can save up to £200 a month towards their first home and the government will boost their savings by 25%, or £50 for every £200, up to a £3,000 bonus.
- b) New streams of funding, such as for low-cost home ownership are intended to be available

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for councils as well as housing associations and private developers. Councils are encouraged to think creatively about the homes they could deliver by accessing some of the new grants.

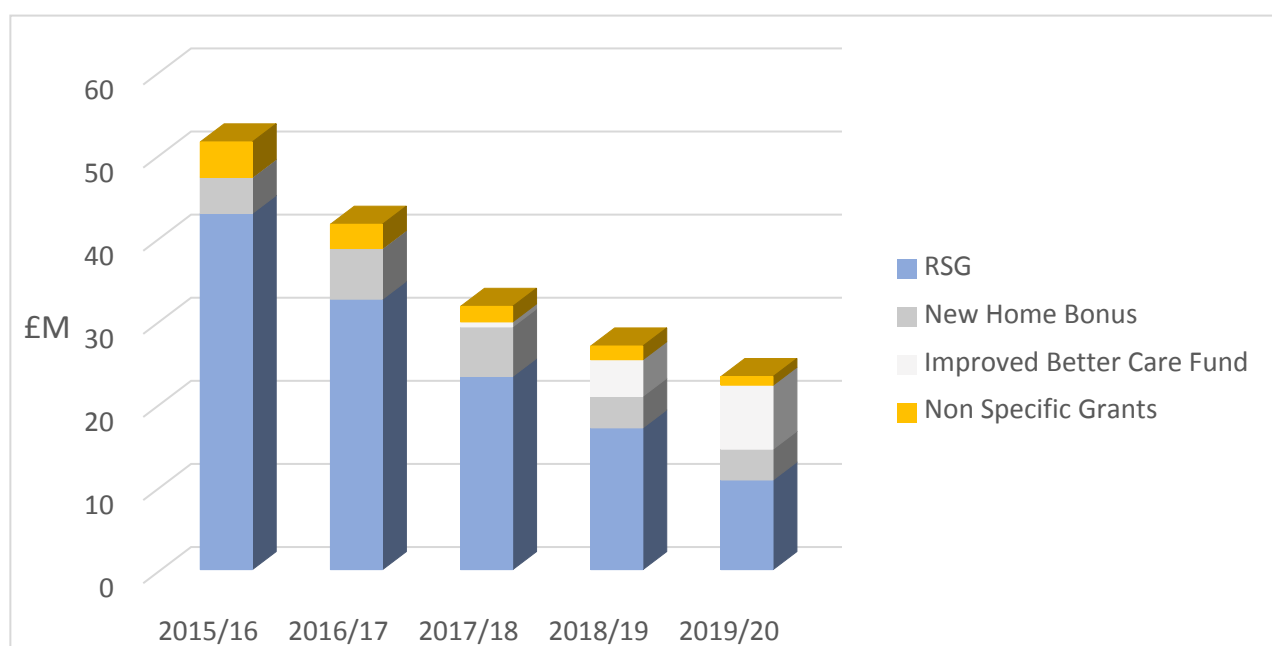
It is anticipated that future disposal or development decisions within the Council will be mindful of the need to consider opportunities to fully utilise all available funding streams and to meet the low-cost starter home commitments.

Provisional Local Government Finance Settlement

Following on from the Autumn Statement, the Government announced the Provisional Local Government Finance Settlement on the 17th December 2015.

This gave proposed local government funding figures for 2016/17 to 2019/20. It also came with the offer for local authorities to receive a four year funding settlement on the production of an Efficiency Strategy, and more detail regarding the flexible use of capital receipts. The settlement looked to redistribute funding to authorities that have social care responsibilities.

For Southampton the impact of the settlement in terms of grant funding can be seen in the graph below. This shows Southampton's grant funding reducing by 55% from 2015/16 to 2019/20



The financial impact of the Provisional Local Government Finance Settlement has been included in the Medium Term Financial Model attached in Appendix 1.

1.4 **Key Assumptions**

Local Authority budgeting is by its very nature difficult to forecast with absolute certainty since there are so many variables that need to be assessed and so much of the information is not known until very late in the process.

Summary of Key Assumptions

Table 1 summarises the key assumptions contained within the Medium Term Financial Model from 2017/18, to arrive at the financial figures presented in Section 3. 2016/17 budgets have been updated to reflect the actual figures and are contained within the figures included in the budget report. Figures in brackets represent a reduction.

Table 1 – Summary of Key Assumptions

Item	2017/18	2018/19	2019/20
Business Rates	1.00%	1.00%	1.00%
Council Tax	3.99%	3.99%	3.99%
Revenue Support Grant	(28.6%)	(26.6%)	(36.7%)
New Homes Bonus	0	(36.2%)	(2.63%)
Other Grants	(38.9%)	(12.2%)	(36.6%)
Consumer Price Index (CPI)	1.8%	1.9%	2.0%
Retail Price Index	3.1%	3.1%	3.2%
Pay Award	1.0%	1.0%	1.0%
Superannuation	13.1%	13.1%	13.1%
Past Service Costs and Compulsory Added Years	8.8%	8.8%	8.8%

Business Rate Retention Scheme

The Business Rate Retention (BRR) Scheme was introduced in April 2013 and represented a major change in the way in which local government is funded. It is seen by the Government as providing a direct link between business rates growth and the amount of money local authorities have available to spend on local services.

Councils are able to retain a proportion of their growth in business rates and will also be taking the risk for reductions in business rates, although there are ‘safety net’ arrangements in place to protect against very large reductions. By the end of this Parliament it is expected there will be a 100% business rates retention alongside additional responsibilities to ensure fiscal neutrality for Central Government.

The scheme as it currently stands means whilst Southampton has no influence over the rateable value, rates charged or the percentage increase each year, it does retain almost half the risk from the volatile nature of the receipts. The one element that the local authority can influence is the economic growth within the region which may result in increased revenues from Business Rates.

The Valuations Office is undertaking a reset of rateable values from 2017/18. This means the level of volatility of business rates in 2017 is at the moment even higher until the outcome of the reset exercise is known.

Businesses can appeal against the rateable value given, and under the new scheme the Council carries approximately half the risk if values are reduced. Appeals can be backdated and as a consequence of this the Council has set aside a provision to deal with this element of the financial impact. In December 2014 the Government announced it was closing the appeals window and that appeals received on or after 1 April 2015 will only be backdated until this date.

During January 2016, a number of local authorities have received requests for 80% mandatory

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relief in respect of NHS trusts. The letter, which was sent by agents GVA is very detailed and is also accompanied by legal opinion from a QC.

The claim being made by agents on behalf of the hospital is for a refund of rates paid back six years (in line with s9 Limitation Act 1980).

In Southampton there are 34 business rated properties which are occupied by NHS trusts, and a letter in respect of local trust has recently been received.

If the agents are successful it would potentially result in up to £9.6M business rates being refunded to NHS trusts locally and a loss of £2.6M business rates pa in future years.

The LGA, supported by SCC, will instruct Leading Counsel this week for advice, to assist local authorities to determine how to deal with the applications.

The current assumption built into the MTFS is fairly neutral, with a 1% increase per annum reflecting the uplift set by the Government. At this stage, no assumptions have been made about growth. This is not because there will be no growth, but because it is difficult to model real growth against downside reductions for displacement, reduced gross rateable value overall due to impact of appeals and business closure. As our evidence base builds on business rates, we anticipate that our modelling will become more sophisticated over time.

Council Tax

The tax base for 2014/15 reflected the required adjustments as a result of the localisation of Council Tax Benefits and changes to associated funding which was implemented from 2013/14.

A new Local Council Tax Scheme (LCTS) was introduced in 2013/14 which, as a result of the localisation of Council Tax Benefits, allows the Council to set its own criteria for offering reduced Council Tax for those eligible.

The changes to discounts, exemptions and LCTS are now in place, and the LCTS administration grant has been confirmed and included in the forecast position.

As set out in Table 1 above, the assumption is that Council Tax rises will be set at just below the 2% referendum limit in future years, at 1.99%. There remains a risk that the Government could impose a lower Council Tax referendum threshold.

Adult Social Care Precept

As set out in the Autumn Spending Review local authorities with adult social care responsibilities can now increase Council Tax by a further 2% adult social care precept. The MTFS assumes this precept will be taken in all years as the calculated increase in funding needed for adult social care far outweighs the income gained from this precept.

Revenue Support Grant Update Post Settlement

Historically a major source of funding for the Council has been the Revenue Support Grant (RSG), however since the austerity measures have been introduced this grant has been reduced drastically with the Council seeing a 28.5% reduction in 2015/16, and a 24.1% reduction in 2016/17. The MTFS reflects the allocations given in the PLGFS.

Housing Benefit Administration Subsidy

In addition to the changes resulting from the localisation of Council Tax Benefits, Housing Benefit is to be phased out and replaced by Universal Credit. As such there was an expectation that Housing Benefit Administration Subsidy, which is funding towards the cost of administering Housing Benefit, may cease from 2016/17.

Confirmation has now been received from the Department for Work & Pensions (DWP) that this funding will continue into 2016/17 whilst the delivery plans for the introduction of the Universal

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Credit are reviewed.

A further £1.2M of non-recurrent grant funding has therefore been assumed in setting the forecast position for 2016/17.

Public Health Grant

The Public Health Grant that was introduced in April 2013, will continue to be a ring-fenced grant to Local Authorities into 2016/17 and 2017/18. The allocation will be subject to a new formula and will incorporate the transfer of funding for Children's 0-5 Public Health services. The final allocation of Public Health grant for 2016/17 is still to be confirmed for local authorities. As part of the spending review it was announced that there would be further reductions in the grant, in addition to the £200M announced for 2015/16, through to 2020/21, as outlined in Table 2 below.

Table 2 – Public Health Grant Reductions

	2016/17	2017/18	2018/19	2019/20	2020/21
Percentage reduction in total grant from 2015/16 baseline	2.2%	2.5%	2.6%	2.6%	0%

The Council is committed to identifying savings from within the total Public Health programme, comprising the delivery of internal and external services, in order to achieve the level of savings required.

Care Act

The Care Act 2014 came into force 1 April 2015. The Act deals with the reform of adult social care and support legislation. The introduction of the Act was to be phased over two years. Changes including the rights of Carers, a national eligibility criteria and universal Deferred Payments which came into force on 1 April 2015. However the changes programmed to come into force from 1 April 2016, including the funding reforms, have now been postponed until at least 2020. This decision was taken nationally in recognition of the overwhelming pressure, across the country, within Adult Social Care services. In recognition of this the government have announced the flexibility for local authorities to increase the council tax by a further 2% as an Adult Social Care precept above the 1.99% referendum limit.

It is currently viewed that the additional burdens introduced from April 2015 have been met within the additional funding provided during 2015/16. It is also assumed for 2016/17 that the continued contribution from the Better Care Fund and funding levels announced within the settlement, although no longer subject to a specific grant, will be sufficient to meet the cost of these responsibilities in 2016/17.

New Homes Bonus

To encourage an increase in the number of homes available in the UK, in 2011 the Government brought in a grant payable to local authorities referred to as the New Homes Bonus. This grant was calculated based on the amount of extra council tax revenue raised for new build homes, conversions and long term empty homes brought into use, with an additional payment for affordable homes. This grant was payable for 6 years.

The PLGFS provided a further update on the scheme with funding confirmed up to and including 2019/20. The funding for 2016/17 will be allocated on the basis of the current methodology, however, consultation is currently underway seeking views on how the funding should be

allocated from 2017/18. Additional funding assumptions have now been included in the medium term financial forecast but due to the uncertainty around methodology, has been included per the allocations provided for within the PLGFS. These are shown in Table 3 below:

Table 3 – New Homes Bonus Allocations

	2016/17 £M	2017/18 £M	2018/19 £M	2019/20 £M
New Homes Bonus Assumption	5.96	5.96	3.80	3.70
Returned Funding	0.14	0.00	0.00	0.00
Total	6.10	5.96	3.80	3.70

Education Services Grant

The Education Services Grant received by local authorities will be reduced in 2016/17 as the per pupil rate has reduced from the 2015/16 level of £87 to £77 for 2016/17. For Southampton this will mean an estimated minimal reduction in grant of £0.30M. The grant is calculated based on several rates per pupil dependant on the type of educational establishment they attend. A decrease in the number of pupils attending maintained schools during the year will adversely affect the grant level. Assumptions regarding the number of schools converting to Academies during 2016/17 indicate that the reduction in grant is more likely to be £0.50M for Southampton.

The longer term view of the Government is that local authorities will no longer run local schools, forecasting this will create a governmental saving of £600M on the Education Services Grant. The estimated impact on Southampton will be a reduction in grant of £1.70M by 2018/19.

Other grants

The Council receives a variety of other grants from Government and the MTFs assumes these will decline over the life of the forecast to circa £0.3M, as per the PLGFS.

The result of these assumptions is that the Council will receive minimal levels of funding from Central Government by the end of the term of the MTFs. This is in line with the PLGFS and the Government's Autumn Statement.

Pay Inflation

Assumptions have been made in the forecast about the likely level of pay inflation that will apply from April 2016. As a large proportion of the Council's expenditure is pay related, this can have a significant impact if actual rates are much higher than predicated.

The previous MTFs model was based on a pay award of 2% per annum, however following the Government's announcement in the summer budget to cap public sector pay awards at 1% this assumption has now been amended to 1% over the medium term.

National Living Wage

The Government's July 2015 budget announcement introduced a new premium for those aged 25 and over leading to a new National Living Wage (NLW) of £7.20 in April 2016. The Government's ambition is for the NLW to increase to 60% of the median earnings by 2020, and it will ask the Low Pay Commission to recommend the premium rate in light of this ambition going forward. Based on Office of Budget Responsibility forecasts, this means the NLW is expected to reach over £9 by 2020.

The Council has adopted the National Living Wage Foundation's recommended living wage, which

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is currently £8.25 (set in November 2015 but implemented by the Council from 1st April 2016), for payment of SCC employees, and this rate is presently higher than the initial NLW.

The Council is mindful of the impact of the NLW on its suppliers, in particular on social care providers, but at present does not intend to alter any of its existing contracts to take account of NLW.

Ending of Contracted out Pensions Schemes

Provision has also been made for the financial impact of changes made to the national pension arrangements which no longer allow National Insurance Rate reductions to public sector employees who opt out of SERPS from 2016/17.

This has been based on the assumption the current staffing levels will continue.

General Inflation

Assumptions have been made in the forecast about the likely level of general inflation that will apply from April 2016. If inflation were to increase at a higher rate than anticipated then this would have an impact on the Council, not least because the Council's major outsourced/partnership contracts are uplifted by indexation linked to inflation on an annual basis.

Current indications are that in the short term an increase is unlikely. However, the risk has been mitigated by the inclusion of amounts in the Risk Fund to cover key elements of inflation, for example in relation to fuel and energy costs, which can be volatile.

Beyond this provision, it is likely that this would be managed as an 'in year' issue and that services would be expected to absorb the difference.

Pension Fund – Past Service Pension Cost and Compulsory Added Years

Employer contributions to the Hampshire Local Government Pension scheme will be reviewed as part of the 2017 triennial revaluation process, with any resulting change in rates applying from April 2017. The position for past service costs and compulsory added years has been included within the forecast for 2016/17 to 2019/20, the using the current valuation from Hampshire County Council an 8.8% per annum increase for the six year period 2014/15 to 2019/20 is assumed within the MTFS Model.

Public Sector Employment – Restrictions on Exit Payments

The Enterprise Bill for 2015 sets up new restrictions on public sector exit payments with a cap of £95,000 being implemented in 2016/17. No date has been stated but is expected to be late summer/early autumn 2016. In addition to a cap being introduced new regulations come into force from April 2016 on the requirement to repay exit payments for up to 12 months after exit payment if further employment is undertaken within the public sector during that time.

In summary:

- Exit payment will be restricted to a cap of £95,000;
- This includes the pension strain costs for all employees aged 55 and over, it is expected that the LGPS regulations will also be amended to limit the liability to the local authority to £95,000;
- Includes redundancy payment, severance or ex-gratia payments, payments for outstanding entitlement such as annual leave owing, compensation under the terms of a contract and pay in lieu of notice; and
- Effective from the 1st April 2016, there will be sliding scale of repayment for any one earning £80,000 or more who returns to public sector employment after 1 day and up to 12 months

after leaving.

The implications for these changes are currently being assessed by HR and Payroll and in consultation with Hampshire County Council. A review is being undertaken of the leavers process and paperwork and the required communication to current leavers earning in excess of £80,000. The financial impact of these changes will be considered in due course and built into future updates of the medium term financial forecast

1.5 **KEY RISKS**

There is a significant degree of risk and uncertainty, arising from both internal and external factors, which could have a significant impact on the key assumptions made within the MTFS. The macro financial systems within which the Council operates is complex and highly sensitive to a range of variables. It is therefore important that those key risks, that could have a material effect on the financial position of the Council, are identified and understood in terms of the potential impact (positive or negative) and the likelihood of occurrence. The foregoing recognises that it is vital to have adequate mechanisms to manage risks if financial stability is to be achieved. These risks are reflected in the assessment and adequacy of detailed estimates and reserves.

Factors that can have a material effect on the financial position of the Council include:

- The lack of certainty in Government funding for future years including grants;
- Changes in function;
- Changes in how services are funded;
- Changes in the economy;
- Changes in Members' priorities;
- Unmanaged service pressures and increases in demand;
- Council tax policy;
- Changes in legislation;
- Level of future pay awards and general inflation assumptions;
- Adequacy of the Risk Fund in any one period;
- Business Rate Volatility and Business Rate Retention;
- Treasury Management and interest rate changes;
- Projected income levels from fees & charges;
- Non achievement of savings;
- Impact of National Living Wage;
- Level of provision for insurances;
- New burdens; and
- Welfare reforms.
- Demographic changes

Risks to the MTFS can clearly therefore arise from both external and internal factors, and it is therefore vital to have adequate mechanisms to manage risks if financial stability is to be achieved.

It is important to note that the revised forecast represents the most realistic forecast position moving forward. However, there are a number of risks associated with these revised forecasts, the main risks being as follows:

1. **Financial Risk** – the majority of the future years' strategy and model is based on a series of assumptions, the further into the future you look the higher the risk that these assumptions are inaccurate.
2. **Political Risk** – The Government are providing more certainty and transparency over central government funding levels for the term to 2019/20. Details to move to 100% Business Rate Retention and the impact of any new burdens that will be imposed on the local authority as a result of that will need to be considered in due course once further clarity and guidance is given.
3. **Treasury Risk**- the MTFFS is based on a stable global financial position going forward with early indications of a recession in the last year of the strategy being taken into account. If this changes it may have a major impact on the financial position of the Council particularly around business rate income, and interest payments. Whilst the Treasury Management Strategy sets the parameters in which borrowing is undertaken a treasury risk reserve of £2M is held to address any transitional costs if it were necessary to undertake a major debt restructuring exercise. Further, a taxation reserve of £2M is held to meet one off shortfall in business rate income as this funding position becomes more reliant on this source of funding.
4. **Transformational Change** – It is essential that the Council undergoes radical transformation to ensure the organisation is fit for future and is sustainable. There is a degree of risk associated with this type of change, particularly as the management capacity to drive this change through reduces, and as we seek to deliver significant change against a backdrop of constrained funding.

2 HORIZON SCANNING

Key issues affecting council services and finances are detailed below as they can have a major impact on the Council's budget in the short and medium term. Annex C provides further context of the demographic and system wide social-economic factors which undoubtedly impact the residents of Southampton and have an impact on the services which the City Council and its partners deliver across the city. Table 6 sets out the financial resources included in the Medium Term Financial Forecast in Annex A to address the factors detailed below, where it has been possible to make a financial assessment at this time. The financial consequences of these items will be reassessed during the MTFFS update in September 2016.

2.1 Demographics

Population forecasts for Southampton and nationally show that average life expectancy is increasing and as a consequence more people are living longer. The fastest growing sector of the population is that aged 65 years and over. Forecasts made using known residential development plans predict the over 65s will rise by 11% between 2011 and 2018 whilst the number of people over 85 years is forecast to grow from 5,300 to 6,000, an increase of 13%. Longer term projections, based on past trends, predict a 42% increase in over 65s in Southampton between 2010 and 2035 with the number of residents in the city aged over 85 reaching 10,000 by 2035.

The increasing proportion of older people creates challenges for individuals and policy makers alike, and it increases pressures on social care resources and other public services. Medical advances mean that people who previously might have died at a young age are living longer, often into adulthood, but do so frequently with long-term conditions and needs which require support to help them live as independently as possible. Likewise, with old age being extended, demands for social care and support are increasing. At the same time, the proportion of the working age population is steadily declining and this may impact on availability of informal and community care.

In 2011/12, 213 older people per 1,000 were in receipt of adult social care services in Southampton

compared to a national average of just 113.5 per 1,000. As more people live longer the number of people living with dementia will continue to rise. It is anticipated that as techniques for diagnosing dementia improve, this will add to the total number of individuals requiring support. In 2011/12 there were 1,439 Southampton residents recorded on GP registers as having dementia; this has increased from 1,022 in 2006/07. This increase represents increasing prevalence and the ageing of the population as well as increased diagnosis and recording by GPs.

2.2 **National and Local Policy**

Welfare reforms and introduction of Universal Credit

Southampton will be in the first tranche of the national roll out of Universal Credit. Once Universal Credit is fully implemented, Local Authorities will be asked to provide 3 main services, mainly to the most vulnerable claimants who have complex support needs. These are:

- Supported on-line access, where claimants need one-to-one support to access the UC claimant portal on gov.uk website or to complete the UC on-line application or both.
- Personal Budgeting Support, where the UC claimant needs support to manage financial affairs on a monthly basis.
- Support for the UC Service Centre for administering the housing element of UC. This includes queries about Housing Benefit and the more complex housing issues that may arise.

'Universal Services – Delivered Locally' will provide the 'partnership framework agreement' for this. Although there have been a range of pilots and projects linked to Universal Credit, it is difficult to predict the direct and indirect impacts locally at this time.

The withdrawal of Central Government funding for Local Welfare Provision will also have an impact on the support the Council and other key services in the city can provide for individuals and household in crisis and for crisis prevention.

Better Care Fund

The Better Care Fund commenced 1 April 2015 and is framed within a formal contract with Southampton City Clinical Commissioning Group for a pooled budget under S75 of the National Health Service Act 2006. The purpose of this Fund is to ensure closer integration between health and social care.

The Southampton Better Care Fund pools funding for a significantly greater number of services than the minimum required which is consistent with the ambition locally to integrate and pool resources at a scale to significantly transform its health and care services. To further meet this aim, plans are being developed to increase the pool and the services provided during 2016/17.

The Southampton Better Care Plan has identified key areas where greater integration between Health and Social Care will make system wide efficiencies that will benefit both organisations. For the Council these efficiencies have been included within the medium term financial forecast.

In addition to the flexibility given to local authorities to raise Council Tax by 2% above the referendum threshold the government have also provided £1.5 billion additional funding for local authorities to spend on adult social care by 2019-20, to be included in an improved Better Care Fund. Taken together, it is estimated that this will provide £3.5BN by 2019/20 to address the demographic pressures facing the social care system. The impact on Southampton of the additional funding through the improved Better Care Fund is shown in the Table 4 below:

Table 4 Additional Better Care funding to be received by Southampton 2016/17 to 2019/20.

2016/17 £M	2017/18 £M	2018/19 £M	2019/20 £M
0.00	0.60	4.40	7.70

2.3 **Socio- Economic Factors**

Children Looked After

There has been an on-going increase in the referrals of children and young people at risk of abuse or neglect over the past few years. Over the period 2010 to 2014, the rate of Children looked after (per 10,000 children aged under 18) has increased by 42.9% in Southampton compared to a 5.3% increase nationally (England average). In the year ending March 2015, Southampton City Council carried out 436.4 Section 47 Child Protection investigations for every 10,000 children (compared with 138.2 per 10,000 nationally) and the city had 101.9 children subject to an initial child protection conference compared with 61.6 per 10,000 nationally.

These high rates in Southampton reflect both the level of need in the City and children's service provision. To ensure that children's needs are met at the earliest stage, a children's services transformation programme is underway. Historically, economic hardship has been linked to pressure on families and increased demand for safeguarding services so there is a very real risk of a worsening situation as the global economic recession and national welfare reforms start to impact.

The financial implications for the city of the number of children in care has continued to be an issue. Since April 2015, the number of Children looked after in the City has remained over 600, when in previous years, the figure stayed between approximately 470 and 590.

The percentage of fostering placements made with independent fostering agencies, (IFA) from April 2014 to December 2015 is approx. 30% (average). The cost of an IFA is, on average two to three times more expensive than an internal placement. This has created and continues to create a significant pressure on the Children Services budget.

IFAs continue to become a greater proportion of the number of looked after children placements than was the case two years ago. We are reviewing our contracts with commissioned IFAs to standardise service provision and pricing structures, allowing us to better predict and manage the future costs of IFA placements. We are also increasing the numbers of 'in-house' foster carers through targeted recruitment, providing more options for in-house placements where appropriate.

The medium term financial forecast incorporates the impact of a reduction in cost of the number of looked after children over the next three years. For 2016/17 the planned trajectory of fostering placement numbers is shown in the Table 5 below.

Table 5 - LAC trajectory 2016/17

Placement/Allowance Type	April 2016	March 2017
In-house Fostering	315	326
IFA	177	154
Residential	23	18
New Independent Living Provision	3	4

Should this projection or an equivalent not be achieved there will be an additional pressure that is not currently allowed for within the councils medium term financial forecast.

2.4 **Physical-environmental factors**

Housing

There are many issues in respect of housing. In Southampton 25% of households live in privately rented housing compared with 17% nationally. Over 7,000 are HMOs. Around 38% or 28,000 private owned or rented homes do not meet the decent homes standard. Nearly a quarter of all homes are in the social rented sector with 17,000 managed by the Council With 14,000 households on its housing waiting list. The cost of housing has increased significantly and there is an affordability issue (house cost-to-average pay ratio). The number of new affordable homes available needs to be increased.

2.5 **Wider Partnership Working**

Community Budgeting

Southampton has trialled a Community Budgeting approach across skills, employment and criminal justice agencies to meet defined collective outcomes on a PBR basis, and the mechanism is still in place to respond to opportunities. The City Deal employment programmes will also be delivered through this route. However, Combined Authority/devolution outcomes are more likely to provide the governance and processes for Community Budgeting in the future.

One Public Estate

Southampton has been involved in the One Public Estate programme that looks to reduce accommodation costs through joint work with other public sector partners as part of the One Public Estate programme. This includes a coordinated redevelopment project involving two health sites, which will achieve considerable estate rationalisation with the opportunity for reduced running costs and land release.

Other key achievements in relation to property rationalisation and partnership working include:

- The partial vacation of the One Guildhall Square building and leasing it to Southampton University from January 2015 which provides an annual income of £0.9M,
- Saving of £0.1M per year from Castle Way,
- A capital receipt of £1.8M from Marland House.

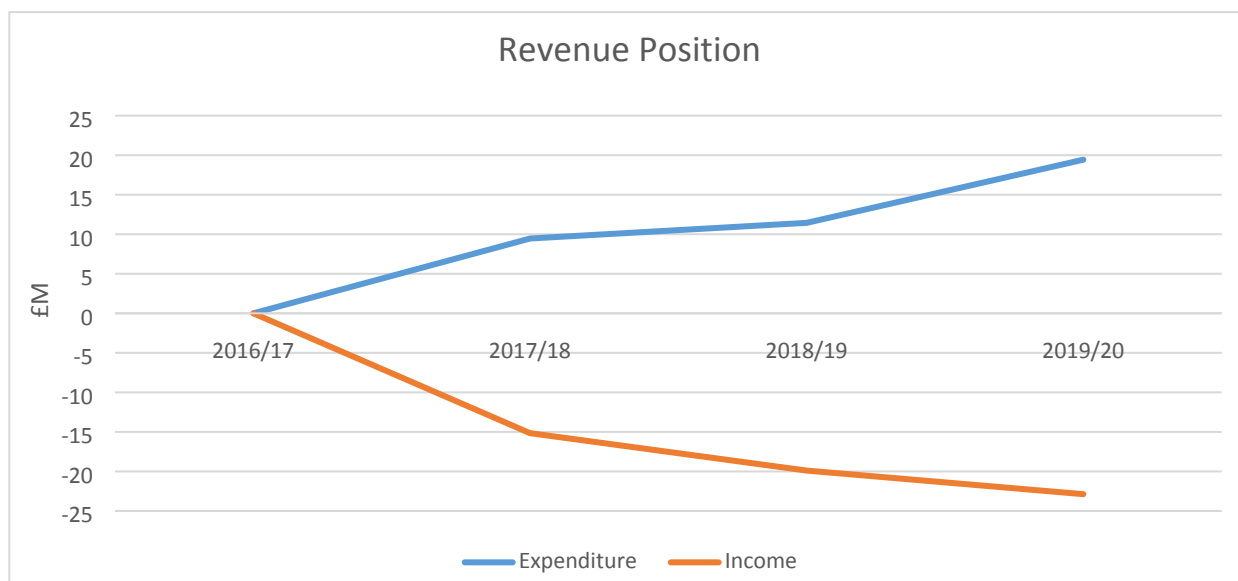
3 **THE FINANCIAL CHALLENGE**

3.1 **Forecast Financial Position 2016/17 – 2019/20**

The Council's forecast financial position is detailed below and includes the implications of the PLGFS, implementation of the transformation agenda, and will be reviewed each year of budget setting to reflect any new pressures and any revision to the Council Strategy.

Where possible factors described in the preceding sections have been built into the financial modelling to ascertain the forecast financial position. The graph below demonstrates the funding gap to 2019/20.

Medium Term Financial Strategy 2015/16 to 2019/20



The current model shows the Council is required to make £42.3M savings over the next 4 years and Table 6 below shows the summary position, with the detail being included in Appendix 2

Table 6 – Summary of Savings Requirements

	2016/17	2017/18	2018/19	2019/20
	£M	£M	£M	£M
Net Expenditure	180.9	190.4	192.4	200.4
Baseline Funding	(180.9)	(165.8)	(161.1)	(158.1)
Savings Requirement	0	24.6	31.3	42.3

3.2 Pressures

Table 7 summarises the pressures included in the forecast from the issues described in the preceding sections as well as pressures that have been identified via the individual service areas through regular financial monitoring and budget setting.

Table 7 – Summary of Pressures

	2016/17	2017/18	2018/19	2019/20
	£M	£M	£M	£M
Demographic	6.3	3.4	2.2	2.4
National/Policy	0.8	2.3	1.0	1.0
Socio- Economic	9.2	0.0	0.0	0.0
Physical-Environment	2.4	0.0	0.0	0.0
Total	18.8	5.7	3.2	3.4

3.3 **New Initiatives**

As well as experiencing pressures the Council have also identified a number of new initiatives that it wishes to undertake to help stimulate the economy. In the main these are being achieved by capital and third party investment in the city for example Cultural Quarter and Watermark.

3.4 **Income Generation**

The Council's approach regarding income generation is to maximise opportunities where possible and income generation forms a key strand of the Transformation programme therefore once proposals are more certain the income generation assumptions contained within the Medium Term Financial Model will be revised.

3.5 **Key Financial Commitments**

The council has in previous years entered into a number of strategic contracts which have resulted in ongoing financial commitment. Whilst these contracts can be monitored and performance managed to ensure they deliver value for money, it can be lengthy and more difficult to renegotiate these contracts to reduce expenditure.

The current commitments are

A) PFI Schools

A PFI contract was approved by the Government to significantly improve the quality of the buildings in three of the City's secondary schools and to provide additional places in two of them. The contract with Pyramid Schools (Southampton) Ltd started on the 29 October 2001 and will terminate on 31 August 2031. The annual fee (Unitary Charge) is £6.426M supported by an income stream (PFI credits from Government) of £3.856M. The DfE have supported the Council in reviewing the PFI contracts with the aim of driving out savings. A significant amount of savings have already been achieved for both the benefit of the schools and the council. A tranche of further savings have been identified and are currently subject to negotiations with Pyramid Schools (Southampton). It is envisaged that these will be finalised during 2016/17.

B) Hampshire Waste Contract

In 1996 the Council entered into a tri-partite arrangement with Hampshire County Council and Portsmouth City Council, in respect of Waste Management Services from Veolia Environment Services. The contract involved the building and running of three Energy Recovery Facilities, two Material Recycling Facilities and the provision of waste management services. The original contract was for a 25 year period until 2025, but it has recently been extended to 2030. The Council is delivering savings in the contract, which has a net value of £7.6M per annum, from 2015/16 onwards due to the agreed contract extension.

C) BUPA Care Homes (Northlands, and Oak Lodge Nursing Homes) Public Private Partnership

The Council has agreed to lease the land, on which the nursing homes have been built, to BUPA for an annual £1 peppercorn rent for 50 years, and has block contracts for 25 years, Northlands until July 2030, and Oak Lodge until 2035.

D) Strategic Services Partnership (SSP)

The Council has outsourced Customer Services, Local Taxation and Benefits, Procurement, Property, Information Technology, Printing, Health and Safety and Human Resources to Capita via the SSP, which commenced on 1 October 2007. The SSP is scheduled to run until 30 September 2022, following an exercise in December 2013 of an option to extend it by five years. The current cost to the Council is circa £20M p.a. for the core fixed contract charges.

E) Highways Service Partnership (HSP)

The HSP with Balfour Beatty commenced on 4 October 2010 and is due to run until 3 October 2020 with options to extend by up to five further years subject to Service Provider performance against Key Strategic Indicators and at the Council's sole discretion. The services covered include highway maintenance, scheme delivery, network management, and winter gritting and asset management.

The annual Lump Sum is currently £2.7M. Current capital and miscellaneous variable spend through the contract is around £10M p.a.

F) Citywatch

The Citywatch contract commenced on 1 October 2012 for a duration of ten years, with extension options of up to five further years at the Council's discretion. The services provided include public safety CCTV cameras and their monitoring, Intelligent Traffic Systems, asset management and asset investment and routine repairs.

The annual Lump sum payment for the services is currently £0.85M.

G) Street Lighting PFI

The Street Lighting PFI is designed to support significant investment in the city's street lighting estate during its first five years of 'Core Investment'. The Government awarded the Council £28M of PFI Credits to replace approximately 16,500 lighting columns and convert 10,250 lantern to create new energy efficient lighting, white light output and install Remote Monitoring and Central Management Systems. The contract commenced on 1 April 2010 and is for a duration of 25 years. The Service Provider is Tay Valley Lighting (Southampton) who sub contract day-to-day management and operations to SSE.

H) Leisure Services

Sports and recreation services are outsourced to Places for People who sub contract operational and day-to-day management to Active Nation. The contract commenced on 1 September 2010 and the term is fifteen years. There is a three year extension option built into the contract. The scope of the contract covers the management of leisure facilities including Bitterne Leisure Centre, The Quays, Chamberlayne Leisure Centre, Woodmill, Southampton Water Activities Centre, the Outdoor Sports Centre, Ski

Medium Term Financial Strategy 2015/16 to 2019/20

Centre and seven outlying sports pitches. The contract includes provision for the Provider to invest £4.5M of capital expenditure over the contract term through a lifecycle budget. The current annual expenditure for the Management Fee is £1.2M.

I) Southampton Guildhall

The Council entered into a contract on 10 February 2003 with Live Nation to manage Southampton Guildhall. The initial term was ten years, extendable by agreement to twenty five years i.e. until 2028. The Council then elected to extend the contract in 2013 for a further ten years and retained the option to extend by a further five years. The net cost of the contract is £0.2M p.a. which consists of a management fee or subsidy of £0.5M less service and energy charges.

J) Sports Development

Sports Development services are provided under contract by Southampton Solent University (SSU) under the banner of Sport Solent. The service promotes and increases sport and physical activity across the City. The contract commenced on 5 December 2011 with a ten year term. The Management Fee is £0.13M p.a.

3.6 Collection Fund

The assumptions made around Council Tax and NDR are reflected initially in the Collection Fund Account, which is a statutory account that records the collection and distribution of taxation.

Following from the assumptions detailed in Section 1.4, the forecast position for the Collection Fund is shown in Table 8 below along with the Southampton City Council share.

Table 8 – Collection Fund Assumptions

	2016/17	2017/18	2018/19	2019/20
	£M	£M	£M	£M
Southampton City Council, Council tax Precept	79.37	80.94	82.49	84.12
Council Tax Adult Social Care Precept	1.58	3.22	4.99	6.82
Business Rates Draw	47.48	47.94	48.42	48.89

3.7 Housing Revenue Account

The national self-financing regime for the Housing Revenue Account (HRA) was introduced in April 2012. A 30 year HRA Business Plan, covering both capital and revenue expenditure projections, has been prepared using the planning principles agreed by Council in November 2011 and amended by subsequent budget reports.

The main points to note are:

- All HRA debt can be repaid over the 30 year life of the Plan.
- The capital spending plans include provision to maintain and improve all existing dwellings and feature an increase in the level of planned expenditure in the early years.
- This investment can be achieved within the Government's borrowing limit of £199.6M, also known as the 'debt cap'. Additionally, a reserve of at least £6M borrowing headroom is retained throughout.
- A provision of £130M is set aside for stock replacement, which will support the renewal of any of the existing dwellings that may be required over the next 30 years. This provision has been phased between year 9 and year 30 of the Plan.
- The revenue budget meets the minimum balances of £2M over the life of the Plan.

The HRA Business Plan has consistently shown revenue balances that increase above minimum levels within the 30 year period. This remains the case, although in the proposed updated plan for 2016/17 onwards the year 30 projected revenue balance will be reduced to £18.8M compared to the equivalent figure of £80.6M in the previous approved Plan. The change is principally due to the impact of a 1% per annum reduction in rents charged to tenants for a 4 year period from 2016 to 2020. This rent reduction is to be imposed by Government in proposals contained within the Welfare Reform and Work Bill 2015/16. The predicted revenue surpluses do not now begin to significantly exceed minimum levels until 2026/27, rather than 2022/23 in the previous plan.

The main risk to the long term plan remains that, if building inflation was to exceed general inflation over a prolonged period, this would have a significant adverse impact on HRA balances. Therefore the surpluses are liable to change annually, either favourably or not, and will reflect the annual review of stock investment needs and estimated unit rates.

In addition, the Housing and Planning Bill 2015/16 sets out a number of proposed changes to Housing legislation which will impact on the current delivery of services to tenants and the resources required to do so. The financial implications of this bill and other potential pressures are described in the Housing Revenue Account Budget Report and Business Plan (*paragraphs 49 to 54*).

3.8 **Capital**

The Capital Programme report details the capital programme for 2015/16 to 2019/20. A high level summary is included in Appendix 2. All the revenue implications of the capital projects have been built into both the General Fund Estimates and Housing Revenue Account Business Plan.

3.9 **Reserves and Balances**

In accordance with the best practice guidance issued by CIPFA, the minimum level of General Fund balances should be reviewed and risk assessed on an annual basis.

The CFO recommends that the minimum level of the General Fund Balances should be £5.5M. This is derived by taking a risk-based approach to assessing the overall General Fund Revenue Account, including reviewing income volatility, interest rate exposure, new contracts, potential overspends in demand led areas such as social care and safeguarding for both adults and children and any other potential issues which may need to be taken into consideration.

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Balances should only be used to fund one-off revenue expenditure; any one-off draw from balances should be prudent, and subject to agreement by the Chief Financial officer. Appendix 2 details the expected level of General Fund Balance going forward after contributions have been made to fund the capital programme and to support the revenue programme. The balance is forecast to be £8.9M at the end of the medium term financial forecast period.

As well as maintaining a risk based General Fund balance the Council can also set aside Earmarked Reserves (for these purposes earmarked reserves excludes school balances) for specific items. Bearing in mind the current pressures detailed in the report the following reserves prioritisation is recommended should any underspends or additional monies become available during each financial year

1. Medium term financial risk reserve – Following on from the compilation of the MTFs, the risks that currently in the funding system, demand pressures and the potential for savings to be delayed as the Council goes through a period of major change, it would be financial sound to set aside monies to mitigate these risks on a non-recurrent basis. This will help to ensure the Council can deal with any pressures whilst it reviews its practices and the medium term financial forecast.
2. Taxation Reserve – due to the volatile nature of business rates and also as the predicted recession in 2019/20 it is suggested the Council looks at setting aside monies to mitigate against any loss if income from both this and council tax, to enable a smoothing of the impact.
3. Transformation Reserve – to ensure the Council can continue to transform and innovate in order to reduce costs whilst improving outcomes, a reserve is set aside to pump prime this transformation.
4. Social Enterprise Fund – to assist staff wishing to set up a social enterprise to run services, subject to meeting a criteria to determine this is the correct future operating model.

A further review of reserves and balances will be undertaken each year as part of the budget setting and final accounts process to ensure the council has adequate resources to cover the uncertainty and risk.

3.10 **Efficiency Strategy**

As part of the Provisional Local Government Finance Settlement announced in December 2015 the Government gave local authorities the offer of a 4 year settlement and additional flexibility regarding the use of capital receipts, providing the Council publish an Efficiency Strategy. The Council already has something similar in the shape of the transformation programme.

Considering the continued financial challenge facing the Council there is an increased need for fundamental, transformational change across the organisation, in both the services it delivers and how it delivers them. This programme is the main driver to ensuring the council has a balanced and sustainable set of services.

The Efficiency Strategy has been developed into a number of streams:

Operating Model – the concept of which was presented to and approved by Council in February 2015 and involved the implementation of a new organisation structure to support outcome based budgeting and reduce budget envelopes. This will be achieved by reducing the top layers of the Council so the Council's structure reflects a smaller number of management layers with broader spans of control. As the Council, is in main, a people driven organisation, a large proportion of our expenditure is linked to staff costs. As such, it is inevitable that the

restructuring in support of the new operating model will need to extend beyond the management tiers mentioned above. Further phases of staff consultation will need to be rolled out in the next financial year and beyond. These will be informed by other transformation initiatives such as those described below and further joined up working and integration of services with partner organisations.

Digital – A fundamental review of the Council’s use of technology, with the objective of positioning this not merely as an essential tool for the delivery of services, but rather an intrinsic part of the Council’s future ‘DNA’. The Council its customers to have an increased and better ability to self-serve, online, at a time that suits them, while ensuring that the requisite support is available for customers who do not have the skills or means to interact with us digitally. The ‘Digital’ programme will be pursued in two elements. The first will initially focus on ‘digitising’ high volume, high cost services in order to drive efficiencies through the automation of process and enhanced levels of integrated workflow solutions. The second element will build on this fundamental step to position the Council as a ‘digital’ organisation by facilitating better integration of services across departments, ensuring better and more seamless customer journeys. These initiatives will enable the Council to operate a leaner structure, whilst also delivering savings in third party spend (with contractors and suppliers) and assets (such as property and office accommodation). These will be through enabled reductions in facility requirements, customer contact structures, consolidation of back office and corporate service functions and retirement of old IT legacy.

Service Excellence – An ‘organisational development’ programme’ that looks to address the need for efficiencies through the deployment of performance management and improvement processes aimed at freeing up staffing capacity as well as service standards, through a planned and better focus on service objective setting, KPI management and measurement, workflow, and agile team based working.

HR policies and procedures – Various efficiency improvement initiatives relating to staffing considerations, including vacancy management, the management of temporary and agency staff, sickness and absence management, and exit process.

Activity Analysis - reviewing the various service activity to ensure efficient and effective delivery of services.

Service Cost Recovery – Cost reduction, minimisation or avoidance activities whose main focus is ensuring that discretionary services provided by the Council are delivered on a basis that either enables the relevant service to recover all of the fixed and variable costs and overheads incurred in the provision of those services, and/or generate the appropriate level of income that is commensurate with the market value of the service being delivered.

Procurement & Contract Management – A review of the Council’s expenditure on third party service provision, including the re-procurement of services to secure better market rates, as well as a more fundamental look and consideration of the actual need for future services and the introduction of measures that can help suppress demand in the first place. As part of this workstream, negotiations are ongoing with the Council’s strategic service delivery partners to deliver further contract efficiencies and savings.

Commercialisation – investigating all opportunities for generating income to the council to replace reducing Government funding.

Prevention and Early Intervention Approach – the Council has also embarked on an programme of reshaping its resources to invest in prevent and early intervention to achieve better outcomes for residents and reduce costs in the longer term. The first areas of focus are social care services for children and adults.

This programme will not be without cost and where it is financially sound to do so the Council will be looking to utilise the new flexibility around capital receipts (Further information regarding this flexibility is contained within the Capital Strategy 2015/16 to 2019/20). Further updates will be presented once more detail is known on the use of this flexibility

Outcomes Based Budgeting

The Council will move to an outcomes based commissioning approach to determine the best way of delivering services, and the aims of budgeting process will follow suit to deliver an outcomes based budget. The Council will review its current expenditure on an outcomes basis and from this baseline point will determine what the appropriate level of spend needs to be to deliver on its agreed priorities, within the financial envelope available.

This is a very different approach to the current one whereby individual services develop savings proposals for consideration by Cabinet and the Council's Management Team, as reflected in the 2015/16 budget report. The sheer scale of the financial challenge ahead will make the current incremental method of finding efficiencies unlikely to identify the level of savings required. Nor will it target resources allocation to the priority outcomes in the most effective way.

Implementing an outcome based budgeting approach will not be a quick process, The timing and approach taken to implement this fundamental review of services will be critical. The outcome based budgeting and commissioning needs to

- Frame the right commissioning question regarding outcomes to determine the service design principals
- Be integrated with the service design gateway process, so that the options appraisals and business cases prepared for services as part of the service design process are consistent with the objectives of this bottom-up review and the commissioning approach (i.e. the fundamental needs and outcomes for the services must be reviewed in addition to scope and delivery model options);
- Not be constrained by the current scope of services and the way things are traditionally done;
- Not be constrained by pre-determined views from within the Council or from models elsewhere;
- Be open to innovation, new ideas and technology and to challenging thinking in relation to how services are scoped, structured and delivered;
- Have political buy-in and be owned at the top level of the Council; and
- Embed the new Operating Model's commissioning principles and approach within the

organisation.

3.11 **Governance Framework for Updating and Monitoring the Medium Term Financial Model**

The Medium Term Financial model is a dynamic model and as such will be changing constantly. It is anticipated that this model will be updated on a quarterly basis via the Quarterly Financial Monitoring Reports. A major review will be undertaken each year and a revised MTFS will be published at the same time. A further review will need to be undertaken each year following the announcement of the Council's settlement funding, when a review of the financial model and assumptions will need to be undertaken.

Both revisions will need to be agreed by Full Council.

3.12 **Managing Budgets and Forecasting**

In setting the annual budget and the MTFS the Council will ensure potential risks are assessed and managed so that their impact is minimised or accounted for either via the Risk Fund, Balances or Earmarked Reserves as is necessary.

Risk Based Budget Monitoring

In year, the Council will monitor its revenue and capital budgets (including the HRA) on a monthly basis and report on a quarterly basis. Budgets will be monitored using a Risk Based approach to budget monitoring using the following principles.

- The focus of Risk Based Budget Monitoring will be on the forecast outturn i.e. forward looking, focused on large high risk or volatile budgets, and will be reported to Cabinet and the Council's Management Team.
- If the in-year budget monitoring gives rise to significant forecast under or overspends, the underlying issues will be considered in terms of likely impact on future year's budgets, and the future year forecasts will be adjusted accordingly as appropriate. The operation of the Risk Fund itself is of course a key factor in monitoring and managing the finances of the Council.

Accountability and Responsibility

Whilst the responsibility lies with Finance for reporting to Cabinet the financial position, the responsibility and accountability for the financial position of the services lies with the budget holder.

All budget holders are responsible for ensuring external income is maximised for their service and for seeking out new opportunities to generate income.

If the budget holder cannot resolve issues within their own service area budgets these should be dealt by Service Directors and Chief Officers.

CONCLUSION

The current forecast position for the Council remains very challenging, whilst it is better than previously expected as a result of the additional funding and flexibilities regarding Adult Social Care Precept. The Council will have seen a reduction in its grant funding of 55% between

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2015/16 and 2019/20 alongside increasing demand for services and funding reducing at an unprecedented rate. This does however produce some opportunities to reshape how the Council currently operates and interact with its customers and this is being explored as part of the Efficiency Strategy and Transformation programme that is already in place.

If the Council is to achieve a £42.3M saving by the end of the period of this Medium Term Financial Strategy, it will need to stop carrying out some services, transform the way in which delivers services, provide less of other services and completely reshape the Council and the way it operates.