GOSPORT BOROUGH COUNCIL

MEDIUM TERM FINANCIAL STRATEGY

2009/10-2013/14

CONTENTS

GOSPORT BOROUGH COUNCIL

MEDIUM TERM FINANCIAL STRATEGY 2009/10-2013/14

1. 0 INTRODUCTION AND OBJECTIVES

1.1 Introduction

The purpose of the Medium Term Financial Strategy (MTFS) is to provide the overall framework for the financial investment in services from 2009-2014. Updated and reviewed at least annually, the MTFS helps to ensure that the Council's financial resources are targeted to achieve the strategic priorities and values contained within the Council's Corporate Plan.

The MTFS also provides a link to other financially related strategies including the Capital Strategy, Asset Management Plan, Treasury Management Strategy and Workforce Development Strategy.

1.2 The Council's Mission

The MTFS plays a key role in helping achieve the Council's mission of *'To work with our community to improve everyone's quality of life and deliver a sustainable future for the Borough.'* by providing an efficient, effective and robust financial framework which will enable the Council to focus resources on its stated priorities.

1.3 Objectives of the Strategy

The main objectives of the Medium Term Financial Strategy are:-

To help ensure that the Council's financial resources are sufficient to achieve its stated objectives within the Corporate Plan including strategic priorities and core values;

To seek to minimise net debt and maximise income in order to provide investment in economic and efficient services within Council Tax increases below the level that might result in the possibility capping by the Government;

To ensure that the Council maintains an adequate level of General Reserves to both meet unforeseen events and help reduce vulnerability to significant fluctuations in Council Tax levels;

To provide both a link and framework to other financially related strategies;

To provide a single document to communicate the financial aims and objectives to staff and stakeholders alike;

Projection of resource requirements over a 5 year period;

2.0 REVENUE

General Fund Base Budget 2009/10

2.1 The current year's budget is divided into the following services:

Gosport Borough Services	Gross Expenditure £'000	Gross Income £'000	Net Budget £'000
Environmental Health Services	1,774	198	1,576
Parks and Leisure Activities	3,448	764	2,684
Housing Services	20,234	19,436	798
Council Housing	11,285	11,346	-61
Refuse Collection	1,817	181	1,636
Town Planning & Development	2,870	814	2,056
Transportation	2,481	853	1,628
Other Services and Expenses	9,098	6,346	2,752
Sub-Total	53,007	39,938	13,069
Transfer from Balances	-97	0	-97
TOTAL	52,910	39,938	12,972

2.2 The net budget for 2009/10 represented a 2.5% Council Tax increase over 2008/09. This can be seen from the following table:-

Gosport-Percentage Council tax increase for 2009/10

Council's additional budget needs	6.8%
Increased Government Grant	-0.7%
Transfer from reserves	-1.8%
	4.3%
Less Council Tax Collection Fund Surplus	-1.8%
	2.5%

2.3 Revenue Budget Projections 2010/11-2013/14

A forecast of the revenue budget for the next four years is shown below and takes into account any significant variations in income and expenditure that are presently known or anticipated. It must be recognised that this projection is subject to considerable variation for a number of reasons such as changes in demand for Council services, new or amended Central Government legislation (including the Government Grant Settlement) and the external economic environment in which the Council has to operate. It is however, still essential that this analysis is undertaken and updated as necessary in order that any potential budget problems or opportunities are quickly identified and the appropriate action undertaken.

PROJECTED GENERAL FUND BUDGET FOR THE YEARS TO 2013/14

		(£'000)			
		2010/11	**20011/12**	**2012/13**	**2013/14**
A	2009/10 Base Budget	12,972	12,972	12,972	12,972
B	Revenue Increases				
	Local Elections	53		53	
	Major Contract re-tendering		350	350	350
	Leisure Centre		-100	-100	-100
	Reserves	50	50	50	50
	Pension Contributions	70	140	210	280
	Other	-6	1	1	1
		167	441	564	581
C	Additional Financing Charges *	156	196	417	451
D	(A+B+C)	13,297	13,609	13,953	14,004
E	Less Revenue Decreases				
	Specific Grants	-114	-189	-189	-189
	Revenue Streams	65	130	175	190
		-49	-59	-14	1
F	**PROJECTED BUDGET TOTALS** (D-E)	13,344	13,668	13,967	14,003
	INFLATION	260	660	1160	1660
	PROJECTED BUDGET TOTALS INCLUDING INFLATION	**13,604**	**14,328**	**15,127**	**15,663**
	BUDGET INCREASE (%)	4.9	5.3	5.6	3.5
	POTENTIAL COUNCIL TAX INCREASE (%)	11.2	9.6	9.7	5.3

***Arising from the Capital Programme**

2.4 Action will be taken to cut the projected cost of services to an affordable level and/or increase income in order to reduce the required Council Tax rises to a level that will avoid capping in coming years. The reductions necessary to the Council's projected General Fund budget to achieve a Council Tax increase of 4.5% (below likely capping level) and incorporating latest inflation projections amount to £376,000 in 2010/11, a further £343,000 in 2011/12 and an additional £402,000 in 2012/13.

General Fund Working Balance

2.5 A key objective of the Strategy is:-

'To ensure that the Council maintains a realistic level of General Reserves to both meet unforeseen events and help stabilise annual fluctuations in Council Tax Levels'

2.6 The Council's Working Balance minimum prudent target level of 7% of net expenditure has been dropped from 2009/10 and the balance frozen at £890,000. It has previously required budget contributions and use of council tax collection fund surpluses in order to maintain the percentage link. Although still very low compared to most local authorities, it is now considered appropriate to cap the Working Balance, subject to annual review of budget risk. This will ease pressure on Council Tax levels slightly and should allow a faster build up of the Revenue Financing Reserve in future for application to spend-to save initiatives etc.

2.7 Gosport's working balance remains in the lower quartile compared to other local authorities. This is considered appropriate as the Council is conscious that the balance represents local taxpayers' funds set-aside and not directly contributing to service provision.

Revenue Financing Reserve

2.8 The Revenue Financing Reserve (RFR) is a provision available for general use, although it is particularly targeted at:-
-reducing exposure to risk by helping to underwrite uninsurable risks and by saving premiums where self insurance is undertaken;
-helping to ensure that variations in annual maintenance requirements can be adequately financed
-helping achieve efficiencies by providing funding for spend to save initiatives.

2.9 It is considered that maintaining a viable RFR is an essential element for improved management of the Council's finances. In order to achieve this, the approved Council policy is that the RFR will receive General Fund Contributions from year end savings, a base budget contribution and Council Tax Collection Fund surpluses (subject to the working balance first being maintained at an appropriate level).

3. HOUSING REVENUE ACCOUNT

Housing Revenue Account (HRA)

3.1 The HRA comprises expenditure and income relating to Council houses and the provision of services to tenants. This includes management and the repair and maintenance of stock and the rent and income from other sources such as housing subsidy.

3.2 The determination of future expenditure patterns relies upon the following key elements:

- Repair and maintenance needs of the stock
- Meeting the decent homes standard
- Aspirations of the tenants
- Rent convergence
- The resources available.

HRA Business Planning

3.3 An HRA business planning model has been developed and covers all the expenditure and income areas listed below for a 10 year period.

- Rental income
- Service charge income
- Garage and other HRA income
- Void levels and rental income forgone
- Mortgage interest
- Management and maintenance expenditure
- Housing Subsidy
- Debt management costs
- Additional expenditure
- Depreciation
- Working balances.

3.4 The plan highlights some of the major issues and pressures affecting the Housing Revenue Account. In particular the level of future rent increases, maintaining adequate balance levels and supporting the costs of maintenance and improvement work on the housing stock will represent major challenges for the future.

HRA Rent Income

3.5 The Council is currently operating its rent setting policy within the national rent restructuring framework which was introduced in 2002/2003.The original aim of this framework was to put all Council house rents on the same clear and transparent basis. It was expected that there would be comparability with Registered Social Landlord rents in the same area and it would take 10 years to achieve this.

3.6 The rent charged would also reflect size of the property, value of the property, average earnings and a percentage uplift to reflect inflation and Government policy. In effect this meant that the Council could not be wholly independent in being able to decide what rent was appropriate for its own area and would be dependent upon Government policy and inflation rates when deciding what rental increase should be applied.

3.7 The Government bases its subsidy calculations on a notional HRA. This notional HRA makes assumptions about the rent levels this Council should be charging. There is currently a variation between the notional HRA rent level assumptions (known as the guideline rent) and actual rents charged to Gosport Council tenants. The difference currently stands at an average of £3.86 rent per week less being charged to Gosport Council tenants than is calculated within the notional HRA. The Government currently calculates that this Council charges £66.72 on average per week over 52 weeks (2009/10). The budgeted charge is £62.86 per week on average. This is partially offset by an average service charge of £1.60 per week.

3.8 The Grant Subsidy system requires a contribution from the HRA calculated on the assumption that this Council charges £66.70 on average per week over 52 weeks. The annual loss to the HRA through not charging tenants at guideline rent is calculated at £380,000.

3.9 It is considered essential that the gap between guideline rents and actual rents is reduced, and the HRA Business Plan assumes from 20011/2012 to 2014/2015 rents will increase at a percentage point above the increase in guideline rent.

Housing Revenue Account Subsidy

3.10 The Housing Revenue Account Subsidy is an assessment of the entitlement to Government support for Council housing based on calculations derived from a 'notional' Housing Revenue Account .In broad terms the Government takes what it believes an Authority needs to spend and deducts from this the income they believe an Authority should raise, this difference being the subsidy entitlement. This Authority's 'notional' income is greater than its notional expenditure, meaning this Authority makes a payment in respect of negative subsidy to the Government. The subsidy settlement for the financial year 2008/2009 was particularly severe for this authority with an additional £1,080,000 payable to the Government.

This was due to a significant increase in notional income (5.37%) whilst notional expenditure remained at the same level as before.

3.11 The draft housing subsidy settlement for the financial year 2009/2010 shows an increase of £360,000 payable to Central Government. This means that this Council will now pay £3.524M in subsidy which equates to £0.34 in every £1 collected. This is primarily due to guideline rents increasing by 6.2%, management and maintenance allowances by only 2.7% and Major Repairs Allowance (MRA) by 4%.The subsidy settlement has used the RPI (Retail Price Index) figure to calculate the guideline rent increase figure and it was measured at 5.1% for the subsidy determination. A 6.8% average rent increase has been approved and will enable maintenance expenditure on Council homes to continue at similar levels and increase the balance of reserves by approximately £60,000 to £479,000. (Due to the anticipated deficit in the revised budget for 2008/2009 it is essential that action is taken to protect the level of HRA reserves in 2009/2010).

Housing Revenue Account working balance

3.12 The HRA working balance is a reserve of the Housing Revenue Account and is “ring fenced” for this purpose.

3.13 The HRA balance as at 31 March 2007 was £168,000 partly as a result of an increase in the amount of repair and maintenance work undertaken in the preceding year which resulted in the budget being exceeded. The balance is significantly lower than the target figure of approximately £800,000 (based on £250 per property). As a result a report was taken to Housing Board in November 2007 outlining a strategy to restore HRA balances to a more acceptable level and an increase in balance levels to £677,000 as at 31 March 2008 was achieved.

3.14 Further expenditure pressures on the Housing Revenue Account have resulted in an estimated reduction of the balance in the current year to £418,000 as at 31 March 2009 (although it is currently predicted this will increase slightly to £479,000 as at 31 March 2010). Although these balance level projections for 2008/09 and 2009/10 represent a significant improvement on the 31 March 2007 figure, it is important that a balance nearer the target level is achieved in the medium to longer term.

Improvement and Repairs

3.15 The Housing services Asset Management Strategy and Action plan 2008 was submitted to Housing Board on 21 January 2009. It is recognised that the full aspirations of this strategy cannot be achieved when taking into account current and predicted Capital resources (as included in the Housing Revenue Account Business Plan).

3.16 A further report is being considered by Housing Board on 4th March 2009 (Housing Repairs Programme 2009/10) regarding the capital investment that can be achieved and outlining where the aspirations of the Asset Management Strategy cannot be met. Analysis of the Council's stock completed by Housing services surveyors during the stock condition survey shows that the level of capital investment over the next 10-15 years equates to £3.6M per annum (at 2007 prices). The Major Repairs Allowance (MRA) is anticipated to be in the region of £2.1M to £2.6M leaving a capital funding gap of between £1M to £1.5M per annum. Work is currently underway to identify how this funding issue can be resolved.

4.0 CAPITAL

Capital Priorities and Selection Process

4.1 In order to ensure that the Council's Capital expenditure is targeted at achieving the Council's Priorities capital projects must be evaluated and prioritised before they are recommended for inclusion in the Draft Capital Programme which is considered by Members as part of the budget process.

4.2 In order to achieve this every proposed scheme is assessed using the Council's *Capital Scheme Proposal Form* which covers a number of key areas of information including examining how the scheme will contribute to the Council's Strategic Priorities and the outputs/outcomes that will be achieved. The form also requires other important information to be detailed including that relating to the cost (both capital and associated revenue implications), funding, programming and risk associated with the project.

4.3 The projects are then considered by the Council's Management Team with particular attention to the contribution to the priorities detailed within the Corporate Plan and associated Corporate Action Statement. The Team then make recommendations to Members on the Schemes to consider and pursue as part of the Council's Capital Programme.

Prudential Framework /Impact on Revenue Account

4.4 The Local Government Act 2003 introduced major changes to the capital funding regime with effect from 1 April 2004.The previous system of controlling Councils capital expenditure by limiting borrowing through the use of credit approvals was replaced by a more flexible system based on affordability.

4.5 The prudential capital finance system (Prudential Framework) allows the Council to make its own borrowing decisions using agreed professional principles as set out in the Prudential Code to ensure that any new borrowing is affordable and prudent.

4.6 The main advantages of the increased freedom to borrow under the Prudential Framework are:-

(i) The ability to bring forward capital schemes that would not otherwise have been possible to fund in the short to medium term under the previous capital financing regime.

(ii) Spend-to-Save Schemes where the cost of the borrowing associated with the capital expenditure on a Scheme can be wholly or partly met by revenue savings arising as a result of the project being carried out.

(iii) The ability to raise funding up to 3 years in advance when market conditions are favourable.

4.7 The expenditure possible under (i) will be limited by the ability of the Council to afford the revenue consequences of the borrowing undertaken. In any event the anticipated low levels of supported borrowing, capital grants and other capital funding resources together with the national pooling of Housing Capital Receipts has resulted in an increase in the need to borrow to finance Capital Expenditure. The anticipated increase in financing charges can be seen within the projected General Fund Budget (paragraph 2.3).

4.8 Projected Expenditure

Capital Programme 2009/10- 2013/14

	2009/10 £,000	2010/11 £,000	2011/12 £,000	2012/13 £,000	2013/14 £,000
Housing (HRA)	2,300	2,474	2,174	2,174	2,174
Housing (General Fund)	1,470	730	730	430	430
Community & Environment	8,866	8,132	1,250	735	35
Policy & Organisation	2,060	321	401	250	250
Total Capital Programme	**14,696**	**11,657**	**4,555**	**3,589**	**2,889**
Major Repairs Allowance - HRA	2,160	2,160	2,160	2,160	2,160
Specific Capital Grants - GF	300	300	300	240	240
Commuted sums-GF	299				
Developer Contributions for Social Housing - GF	980	300	300		
Other Grants and Contributions - GF	4,896	967		350	
Anticipated Capital Receipts -GF	4,163	3,065	1,265	225	225
Local Resources - Prudential Borrowing - GF	1,798	4,551	516	600	250
Local Resources - Prudential Borrowing - HRA	100	314	14	14	14
Total Capital Funding	**14,696**	**11,657**	**4,555**	**3,589**	**2,889**

4.9 A significant proportion of the planned capital expenditure relates to the Community and Environment Board, the main schemes being the new Holbrook Recreation Centre and the replacement of the Landing Stage.

5.0 TREASURY MANAGEMENT STRATEGY

5.1 The treasury management service is an important part of the overall financial management of the Council's affairs. Its importance has increased as a result of the freedoms provided by the Prudential Code. Whilst the prudential indicators above consider the affordability and impact of capital expenditure decisions, the treasury service covers the effective funding of these decisions. There are also specific treasury prudential indicators.

5.2 The Council's activities are strictly regulated by statutory requirements and a professional code of practice (the CIPFA Code of Practice on Treasury Management).

5.3 An annual strategy is required to be recommended to Council outlining the expected treasury activity for the forthcoming 3 years and a further report is produced after the year-end to report on actual activity for the year. This report includes the Treasury Management Strategy for 2009/2010.

5.4 A key requirement is to explain both the risks associated with the treasury service and how those risks are to be managed.

This strategy covers:

- The current treasury position

- The expected movement in interest rates
- The Council's borrowing and debt strategy
- The Council's investment strategy (in compliance with the DCLG guidance)
- Treasury performance indicators

5.5 Treasury Position

The council had a net investment of £1.823M at 31 March 2008 which is forecast to increase to £2.904M at 31 March 2009.

In view of the uncertainties and higher risk levels that have recently developed in the money markets, a very risk averse policy is being operated that is substantially within the parameters set by Council. Current emphasis is on security and liquidity at the expense of revenue returns.

The authority to respond to different interest rates throughout the financial year is delegated to the Borough Treasurer. In his absence the Council's response to short term fluctuations is jointly agreed between any two of the Financial Services Manager, the Head of Accountancy, and the Group Accountant. There is a clear segregation of duties between setting up and authorising loans and investments.

In 2008/09 to date, the Council has been in a net investment position. This is expected to move to a net borrowing position in line with capital programme projections although the speed and degree of this will depend on the progress with capital schemes, the success in raising capital receipts and the uncertainties of the economic recovery.

Maturing investments in 2009/10 will be required to fund the capital programme and the projected need for available cash resources will be balanced against new capital receipts and the availability of low rates of interest for long term loans through the Public Works Loans Board. <u>The robust management of capital budgets and schemes is a prerequisite to forward planning to ensure the availability of cash resources.</u>

There is a clear operational difficulty arising from the current banking crisis. Ideally investments would be invested longer to secure better returns, however uncertainty over counterparty creditworthiness suggests shorter dated investments would provide lower exposure to risks.

Expected Movement in Interest Rates

The UK economy has entered a profound recession, worsened by a dangerous combination of negative growth and dislocation in the domestic and world financial markets. The situation in the economy is considered critical by the policy setters who are concerned that the testing financial environment, the sharp decline in house prices and persistently tight credit conditions could trigger a collapse in consumer confidence. At best this could deliver a short, sharp downturn, at worst a prolonged Japanese-style recession.

The Bank is expected to continue to ease policy and the need to drive commercial interest rates, currently underpinned by the illiquidity of the money market, to much lower levels suggests the approach will be more aggressive than might otherwise have been the case. Only when the markets return to some semblance of normality will official rates be edged higher.

- **Borrowing and Debt Strategy 2009/10 – 2010/11**

The growing uncertainty over future interest rates increases the risks associated with treasury activity. As a result the Council will take a cautious approach to its treasury strategy.

The Borough Treasurer, under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time, taking into account the risks shown in the forecast above.

- All long-term loans (in excess of 365 days) to be raised through the PWLB, Bond Issue or Loan Receipt (1989 Housing Act).
- All short term loans (less than 365 days) to be raised through dealings on the London Money Markets using
  - Garban Harlow Ueda Limited,
  - Tradition UK Limited
  - ICAP
  - R P Martins
  - Other brokers at the discretion of the Borough Treasurer
  - Or Directly via the Council's bank

Returns are to be maximised by efficiency rather than risk – primarily by enhanced monitoring of capital projects and cash flows.

- **Investment Strategy 2009/10 – 2011/12**

- In order to limit interest rate exposure all investments are to be fixed rate transactions
- No Investments to exceed 364 days
- A £3m limit with any single body
- A minimum credit rating with Moodys Credit Rating Agency of P1 Short Term, Aa3 Long Term. Credit ratings are monitored closely on at least a weekly basis.
- Investments to be placed with
  - The Nationwide, Britannia and Yorkshire mutual / building societies, (biggest 3)
  - Irish Banks (The January 2007 policy amendment to invest with Irish banks was not carried forward to the January 2008 policy statement due to an oversight and this is now corrected to

formalise current lending. No further investments will be made in these institutions in the foreseeable future)

- o Short term surplus funds are to be invested in money market funds or deposit accounts as operated by the Council's bank, these offer immediate deposit and withdrawal facilities but still at advantageous rates of interest.
- o The main principles governing the Council's investment criteria are the security and liquidity of its investments, although the yield or return on the investment will be a consideration, subject to adequate security and liquidity.

6.0 BUDGET STRATEGY AND PROCESS

6.1 The Council's Corporate Plan 2005-2008 was approved by Full Council in October 2005. The Council's Strategic Priorities are categorised under four main headings namely, People, Places, Prosperity and the Pursuit of Excellence (contained within the Corporate Plan). An update of the plan for 2009-12 is currently being prepared.

The Corporate Action Statements (contained within the Corporate plan) underpin the delivery of the Corporate Priorities. Any budgetary implications arising from the actions outlined in Service Improvement Plans are included within the Council's initial Draft Budget. Depending on the resource constraints affecting the Council these are either ultimately approved or if this is not possible the unit SIP is amended to reflect this.

There is a statutory requirement to produce a robust balanced budget with formal consideration of reserve levels.
Budget preparation will commence in July and will incorporate requirements resulting from Council priorities identified from Capital Strategies, Community Strategy, Corporate Plan and Best Value action plans.

6.2 Budget preparation commences annually in July and culminates in recommendations to Boards and Council the following January/February.

6.3 Budget preparation is "zero-based" where appropriate and new bids are minimised. Maintenance proposals are provided for according to the latest Asset Management Planning requirements.

6.4 Prudent inflation parameters are used in the build up of the initial budgets.
(It should be noted that many areas of the Council's expenditure e.g. contracts, are subject to inflationary pressures that can substantially exceed general inflation.)

6.5 One-off sources of income will not be used to fund ongoing base expenditure requirements.

6.6 There is a need to consider and prioritise capital projects within the Capital Programme and consider affordability, including impact on local tax levels as part of the Budget Process.

6.7 Once the Council's budget is set and the precepting authorities' requirements known Council set Council Tax levels for the forthcoming year. This has to be done by 11 March.

6.8 In the interest of sustainability, the Council will not generally budget to use one-off or short-term revenue grants on expenditure that is properly part of its base budget requirements.

7.0 RISK MANAGEMENT AND INSURANCE

7.1 Risk Management

7.1.1 The Council recognises the importance of an effective risk management process covering all aspects of the significant business risks that the authority faces. Although much has already been achieved, further development of the risk management process remains a key priority of the Council and significant resource has been earmarked for this purpose.

7.1.2 The Council has an agreed Risk Management Strategy in place. All capital schemes must be risk assessed as part of the approval process. In addition a risk register is in operation that assesses financial risks as part of its overall framework. Finally, a corporate risk management group meets bi-monthly to discuss key risk issues that influence the Council's day to day business and to further develop and critically review the risk management process.

7.1.3 The Budget report to Council and the Budget Book highlights the principal areas of risk with an assessment of likelihood and impact on the budget.

7.2 Insurance

7.2.1 The Council has a range of insurance policies which help safeguard against many of the higher financial risk areas particularly relating to property and public liability insurance.
The general insurance market has seen marked increases in premiums in recent years and this together with a poor recent claims history has led to the cost of this Council's insurance portfolio increasing significantly. The Council is, however,

currently in the process of tendering its insurance portfolio and it is considered likely that an improvement in the competition in the Local Authority Insurance market together with the Council's improving claims history will result in future insurance premium savings.

7.2.2 The Risk Management Group monitors recent claims to ascertain any patterns and seek appropriate preventative measures.