Committee:	Date:	Classification:	Report No.	Agenda Item
Overview & Scrutiny Cabinet	28th July 2009 29th July 2009	Unrestricted		8.1

Report of:	Title:
Corporate Director - Resources **Originating Officer:** Alan Finch, Service Head Corporate Finance	**Resource Allocation and Budget Review 2010/11- 2012/13** **Ward(s) Affected** All

1. SUMMARY

1.1 In February 2008, the authority established its first ever three year budget, which set balanced budgets for the three financial years beginning in April 2008 and ending in March 2011. The three year budget was rolled forward last year, with the main focus of attention shifting to significantly improving service delivery in priority areas and further commitments to Service Improvement Growth and capital investment for the current financial year were made in setting the 2009/10 budget.

1.2 This report begins the budget process for 2010/11, the final year of the three year budget, with the intention of setting the Council Tax for that year on the 3rd March 2010. The report also considers how the Council can maximise the value it receives from public money through medium term planning, greater scrutiny of spending, and focusing resources on the priorities in the Community Plan 2020. The Council also needs to consider the medium term risks and issues that will arise during the course of the current three year strategy and which may impact upon the next.

1.3. We now face the most uncertain economic conditions for some years. Since last year's Financial Outlook report the country has entered a recession and the banking crisis has set in train events which are likely to lead to that recession being a particularly long and deep one. The public finances are now severely in deficit and all three main political parties have made it clear in their statements that growth in public spending will need to be curtailed from the levels experienced over recent years in order to bring public finances back into balance. In view of these emerging issues, and others set out in the report, it will be necessary to revisit assumptions in the three-year plan and to reassess risks. The report explains these issues in greater detail and concludes that an additional savings target will be necessary in 2010/11 in order to ensure a balanced budget and provide the opportunity for policy decisions around the budget.

1.4. The report also covers plans for capital investment in local assets and infrastructure, which are inseparable from those which concern the day-to-day running of services, and considers that further asset disposals are likely to be necessary if targeted investment in local priorities is required.

1.5. As previously reported, the Comprehensive Spending Review and review of grant distribution which was implemented in 2008 leaves the authority at the Formula Grant floor for the foreseeable future. The annual increase in funding will not be sufficient to meet the cost of inflation and projected population growth. In addition, this year the Government has yet to make announcements about specific grants for 2010/11.

1.6. The report identifies the planning parameters which should apply to strategic and resource planning for 2010/11- 2012/13, with the overall aim of providing sufficient flexibility to deal with risk and provide scope for a degree of policy choice, and invites Cabinet to consider a strategy for meeting a balanced budget for the period.

2. RECOMMENDATIONS

Overview & Scrutiny Committee is recommended to consider the report and pass any comments it wishes to make to Cabinet

Cabinet is recommended to:

2.1. Consider the financial outlook and medium term projection set out in this report.

2.2. Note the comments on revenue budget inflation and determine an approach to funding inflation in the budget strategy.

2.3. Note the outcome of the review of the budget forecast for 2010/11 and officers advice on the risks of additional costs falling in 2010/11 which may not be covered by mitigating measures to be undertaken, and note the Medium Term Financial forecast for 2011/12-2012/13.

2.4 Note the resources provisionally available to fund the capital programme.

2.5. Note the position in relation to the Housing Revenue Account.

2.6. Determine a budget strategy for 2010/11 and agree that Corporate Directors prepare service and financial planning submissions in accordance with agreed parameters, and the outline process and timetable set out in section 9 of the report.

3. BACKGROUND

3.1 The Council operates a sound resource allocation process underpinned by an integrated strategic and resource planning framework. Processes are designed to ensure that:

- Service plans are developed against the background of forward looking financial forecasts
- The financial consequences of proposed actions are identified and are seen as an integral part of service planning
- Financial plans allocate resources to address changing community needs and priorities.

3.2. Medium term financial planning is an essential component of the Council's strategic and resource planning framework. While many key decisions, including the formal setting of Council Tax, will continue to be taken annually, those decisions need to be set in the context of a longer term planning horizon. Forward planning offers greater opportunity to link service and financial planning.

3.3 The Prudential Borrowing system also requires the Council to be clear about its proposed capital spending plans for three years ahead and explicit about the impact of the associated financing costs on Council Tax.

3.4 2010/11 is the final year of the Government's three year financial settlement covering the period 2008/09- 2010/11. This applied to the main Formula Grant and to Area Based Grant, and has enabled local authorities to plan ahead and ensure more effective and efficient use of resources. Unfortunately, so far there has been no announcement from Government of funding beyond 2010/11, and as a result local authorities will need to plan with greater caution.

3.5 The report is intended to provide the context for the development of the detailed budget proposals in the coming months.

4. REVIEW OF BUDGET FOR 2010/11- 2012/13

4.1 Process and Principles

This current report provides forecasts for a three-year plan covering 2010/11-2012/13, covering three main areas;

- Building 2008/09 financial results (known as 'outturn') into the three-year forecast, and;
- Reviewing the budgets already set for 2009/10 and 2010/11 and the forecast for 2011/12 and building in to forecasts issues which have emerged since the three year budget was set.

4.2 **Financial Outturn 2008/09**

4.2.1. Elsewhere on this agenda, the Cabinet is receiving a report setting out the financial outturn for the General Fund and Housing Revenue Account. These can be summarised as follows;

	2008/09 surplus	**2008/09 deficit**	**Balances as at 31st March 2009**
General Fund	£1.6m		£27.1m
Housing Revenue Account (HRA)		£11.9m	£23.3m

4.2.2. The surplus on the General Fund was largely brought about by actions taken during the year to contain expenditure. The HRA deficit was largely planned for and results from priority spending on environmental improvements to estates as well as costs associated with the reorganisation of the Housing Services that came with the setting up of Tower Hamlets Homes.

4.2.3 The Council's current financial position remains sound, but will require continuous assessment and vigilance in the light of the pressures and issues identified in this report.

4.2.4. The way this should be seen is that the Council's overall financial health places it in a good position to face the recession and to manage the fact that the authority's funding from Government will grow by less than the rate of inflation for the foreseeable future. The authority is in a strong position to face this situation providing key decisions are taken at the appropriate time.

4.3. Review of Budget and Medium Term Financial Plan 2009/10- 2011/12.

4.3.1. The three year General Fund budget established for 2009/10- 2011/12 is set out at **Appendix A**. The budget set by Council for 2009/10 on 4th March 2009 was £297.926m and this is therefore the base budget for all subsequent budget decisions.

4.3.2 Inflation

For 2010/11- 2012/13 estimates of the cost of funding inflation in the General Fund have been prepared on the following basis:

- 2.25% for pay, which is slightly above the Government's target for public sector pay increases of 2%.
- 2.50% for general costs.

The forecast breaks down as follows;

Figures in £m	**2010/11**	**2011/12**	**2012/13**
Pay	3.19	3.45	3.54
Non Pay	3.30	3.58	3.66
Total	**6.49**	**7.03**	**7.20**

4.3.3 The Government continues to maintain an inflation target of 2%, but inflationary pressures in the economy have become more unpredictable than they have been over recent years. Prices are currently falling, although not as quickly as in recent months, and there is the possibility that economic recovery when it comes will bring higher inflation. Forecasts at or close to Government targets would therefore seem to be appropriate for the Medium Term Financial Plan.

4.3.4. If inflation is higher than anticipated, the current level of general reserves currently held by the authority would allow risks to be managed in the short term. In view of this, officers recommend that, at this stage, the three year budget should not be amended to allow for higher inflation, but any increase in costs should be managed within the budgets set.

4.3.5. The 2009/10 budget includes provision for pay awards to staff of 2.25%. However, the Local Government Employers have made a pay offer of 0.5% for 2009 which as been rejected by the Unions. In view of this, pay inflation has not been allocated to Directorate budgets and it remains held centrally as a contingency.

4.3.6. Notwithstanding the prospects for inflation, in the event that savings are required in the early years of the Medium Term Financial Plan, one way of doing this would be reduce the provision for inflation in the budget. This would leave officers to manage within a budget cash limit which did not make full provision for inflation; however, inflation would still arise, so officers would need to make decisions in year which would bear down on the costs of services without affecting front line services.

4.4 Committed Growth Pressures

4.4.1. Committed Growth is the unavoidable cost of maintaining services at existing levels, taking account of demographic change, new legislation or other unavoidable factors.

4.4.2. The Committed growth that has been agreed in budgets for 2009/10 – 2011/12 is set out at **Appendix B1**. The main service areas of committed growth over the next three years are;

- Social Care Commissioning
- Waste Management
- Local Development Framework

4.4.3. The Medium Term Financial Plan for 2010/11 also includes the impact in that year of two items brought to Members' attention in setting the budget for 2009/10.

- A further tranche of the increase in the **levy to the London Pensions Fund Authority** in respect of the pensions deficit for former GLC and ILEA staff.

- The estimated impact of the downturn in the economy on **capital financing and investment income,** where as Members will recall the net cost is expected to increase, largely because of the loss of income from historically low interest rates. This forecast will be kept under review during the budget process.

4.4.4. As the Medium Term projections were produced some months ago, it is important to confirm that the assumptions behind them are still relevant. Officers have therefore been reviewing these assumptions over recent weeks to ensure that they are valid. It should be stressed that the figures for future years in particular remain provisional and could be understated.

4.4.5 The following issues have emerged which have an impact on the budget for 2010/11 and the committed growth forecasts for 2011/12- 2012/13 and details of these are provided at **Appendix B2**

4.4.6**. Adults, Health & Wellbeing**

Committed Growth projections for learning disabilities commissioning and older people with dementia have been revised downwards by £200,000 in 2010/11.

4.4.7. **Communities, Localities & Culture**

The Directorate has identified an additional growth item of £378,000 relating to the costs of the Anti Social Behaviour, which can no longer be charged to the Housing Revenue Account. The Directorate is in the process of identifying savings to cover this growth.

4.4.8**. Development & Renewal**

One savings item has been identified which will not be achieved;

	2010/11 £000s
Digitisation project	100
	100

The Directorate has identified alternative savings to the General Fund of £100,000 to match this as follows;

	2010/11 £000s	Comments
Energy management – charge for services	100	Further information is required as to the impact of these proposed charges on the rest of the organisation.

4.4.9. **Resources/ Adult Services**

	2010/11 £000s
Housing Benefits/ Homelessness: change in subsidy arrangements affecting homelessness	986
	986

It is expected that during the Summer the Government will introduce new rules for benefit subsidy which reduce the subsidy available on accommodation for the homeless. The proposals stem from the Government's belief that the market for homeless accommodation is distorted by the fact that landlords know they can recover rents up to a threshold through the benefits system. In practice, when these new rules are introduced, they will potentially need to be tackled by a combination of actions by Resources and Adults, Health & Wellbeing (which is now responsible for homelessness). The anticipated cost of this is £986,000.

The intention is to seek a response from landlords to accept reduced rents, bringing them more into line with the subsidy levels. It is not known how successful this will be, and for now it is prudent to assume that an additional cost will be incurred by the authority.

4.4.10. **Corporate**

	2010/11 £000s	2011/12 £000s
Office accommodation; inflationary pressures.	360	260
Office accommodation; risk of failing to deliver planned savings	1,420	1,420
	1,780	**1,680**

In relation to **Office Accommodation**, the budget pressure arises in two ways. The inflationary pressure is largely due to contractual rent reviews. In addition, the Medium Term Financial Plan currently allows for £1,420,000 in savings arising from the Office Accommodation Strategy over the next two financial years; 2009/10 and 2010/11. The budgets have already been removed from facilities management as part of the office accommodation strategy. The service will however continue to incur spend unless or until the budgets are reinstated or the reason for the spend (ie the demolition or disposal of a property) occurs. However, the dramatic downturn in the property market among other factors has resulted in a delay in delivering these savings.

Officers are developing proposals to address this pressure and this issue has recently been discussed at the Capital & Asset Management Board. At this stage, however, Members are advised that the authority needs to plan on the basis that some or all of these proposals may not be deliverable within the short timescale required. A further update will be provided later in the budget process.

One further area has been identified where it is not possible at this stage to identify the financial impact;

	Comments
Carbon Management – risk of fines and losses on carbon trading	The authority becomes subject to the national Carbon Trading scheme with effect from 2010/11. Depending upon our performance relative to other organisations, the authority may either receive a fine or levy, or a reward. The maximum amount of fine anticipated in 2010/11 is £700,000, which potentially increases in later years.

It is not considered at this stage that funding be set aside explicitly in the budget; however, the risk assessment which informs decisions on the level of reserves will need to take account of the Carbon Management scheme. This is a matter for later in the budget process once a fuller picture of the risk is available.

4.4.11 **Summary**

The 'due diligence' exercise has therefore identified the potential for up to £2.566m worth of additional growth in 2010/11, and although actions are being undertaken to offset this growth, there is a substantial risk that these will not bear fruit. Members will need to consider these risks in determining a budget strategy and further officer advice in this regard is set out later in the report.

	2010/11 £000s
Adults, Health & Wellbeing	-200
Office Accommodation	1,780
Housing Benefits/ Homelessness	986
	2,566

4.5. Savings Identified for 2008/09 to 2010/11

As part of the budget process for 2007/08, Directorates were asked to identify savings proposals for further savings in 2009/10 and 2010/11. The approved savings for 2010/11 are listed at **Appendix C1**. Officers have reviewed these proposals and advise there are no serious and unmanageable risks affecting the delivery of these savings at present. However this position will be kept under review.

Two savings proposals previously put totalling £562,000 have been withdrawn by the Communities, Localities and Culture Directorate, one relating to parking and one to leisure, and these have been replaced with two alternative proposals in the same services. Details of these are attached at **Appendix C2**

4.6 Service Improvement Growth

Appendix D summarises the Service Improvement Growth agreed in the Three Year Budget.

4.7 Resource Projections

Formula Grant

4.7.1. The main grant contributing towards the authority's General Fund revenue budget is Formula Grant. A grant figure has been announced for 2010/11 and this is shown in the table below.

	2009/10 £m	2010/11 £m
Formula Grant	228.816	232.204
Annual Increase %	1.7%	1.5%

4.7.2. The authority's grant settlement is at the minimum level allowed for by Government, known as the 'grant floor'. This is because grant distribution changes introduced in 2007 had a severely detrimental effect on the authority's grant settlement. The floor is intended to protect the authority from the worst effects of this change by phasing in its impact. In this case it is estimated that the authority will remain at the grant floor until around 2014/15. This position may change subject to the latest review of grant distribution which is current underway and which is due to be introduced with effect from 2011/12. However there is nothing in the proposals at the moment to suggest that the Council will not remain at the grant floor for a period beyond the end of the current Medium Term Financial Plan.

4.7.3 The grant floor is normally set at a level below inflation. The practical impact of the floor, therefore, is that the authority is likely to receive grant increases at below the rate of inflation for some years, and in practice no funding towards the costs of population growth.

4.7.4. No announcement has been made of Formula Grant figures for 2011/12 onwards. In view of the public spending forecasts included in the Chancellor's budget in April, the independent Institute for Fiscal Studies has calculated that there could no grant increase in cash terms for most public services over the period of the next Spending Review. Medium term forecasts have therefore been prepared on the basis of no increase in Formula Grant for the three years 2011/12 - 2013/14, although this could also prove to be optimistic.

Area Based Grant

4.7.5 In 2008, the Government introduced a new form of grant called Area Based Grant. In practice this did not mean Councils received extra money, because the ABG was created by combining around 40 former specific grants. The Council's allocation for 2010/11, which has not been finally confirmed by the Government, is £18.815m, excluding the Working Neighbourhoods Fund.

4.7.6. Area Based Grant is not ring-fenced, and a review of services paid for from specific grants combined into ABG took place during 2008 to review how these grants are used to deliver services, to ensure that they are used efficiently and effectively, and are focused on Council priorities. This exercise resulted in savings of £3.5m in 2009;10 and £3.8m in 2010/11 which have been allocated to other priorities in the Medium Term Plan.

4.7.7 No Area Based Grant announcement has been made for 2011/12 or beyond.

4.7.8. The Working Neighbourhoods Fund is part of the ABG, but since tackling worklessness is a particularly high priority for the Council, especially in the current economy, the Cabinet decided to treat this grant separately. Consequently, a priority-led strategic commissioning process has been put in place to allocate this grant and in February 2009, Members made decisions to allocate £20.111m of grant in 2009/10 and 2010/11. This left a balance of £3.539m which is therefore available for other priorities, although because WNF is only allocated by the Government up to the end of 2010/11, this must be regarded as a one-off funding, and not ongoing. There are proposals elsewhere on this agenda to allocate up to £0.273m to support a bid to the Future Jobs Fund which if approved would leave £3.266m.

4.8 Other Specific Grants

A number of specific grants have been announced for 2010/11, but unlike Formula Grant, there is no commitment from the Government to stick with these pre-announced figures. The assumption built into these forecasts is that specific grants will continue to be available beyond the end of 2010/11 although again this will be subject to review. The availability of specific grants must therefore be considered a risk for this budget process. Final allocations for grant for 2010/11 will not be announced until November 2009.

4.9. Dedicated Schools Grant

The Government introduced the Dedicated Schools Grant to fund schools budgets in 2006/07. The grant is announced on an annual basis, with a provisional sum announced in November or December in the year before the start of the financial year to which it applies, and final figures the following May once the school census has taken place. The schools budget needs to be set in accordance with the grants allocated.

4.10 Local Area Agreement

4.10.1 The Local Area Agreement to deliver a broad range of outcomes agreed between the Tower Hamlets Partnership and the Government Office for London began in April 2006 and is now in its third and final year.

4.10.2. Success in achieving the Local Area Agreement results in the payment of a Reward Grant and the authority will receive £4.696m in two equal instalments in 2009/10 and 2010/11, half of which (£2.348m) will be paid as capital grant and is therefore available only for capital spending, and half of which is paid as revenue grant. This funding is also available for one-off spending priorities.

4.11 Parking Control Account

The Parking Control Account is in surplus by £957,000 as at 31st March 2009 and officers advise that this sum is also available for one-off purposes.

4.12. <u>Council Tax</u>

4.12.1. The three year budget includes a general assumption that Council Tax will rise by 2.5% a year throughout the period. In practice, the Council Tax is agreed by the Council on an annual basis and the 2.5% used in these forecasts is simply a planning assumption and will be subject to amendment by Cabinet and Council.

4.12.2. The marginal amount raised for each 1% increase in Council Tax in 2010/11 is estimated at £0.715m. Correspondingly, each 1% reduction in Council Tax would require additional savings to be made of this same amount.

4.13 Other Issues and Risks

4.13.1 <u>Collection Fund</u>

Council Tax collected on behalf of the Council and the Greater London Authority is paid into the Collection Fund. Any surplus on the fund is available to the authorities to reduce the Council Tax in future years; any deficit must in turn be recovered from Council Tax. It should be noted that the aim each year is to equalise the fund, so the amount required as a contribution or available from redistribution should be zero.

In recent years, historic surpluses and significant growth in the Council Tax base have ensured that the Collection Fund has been in surplus each year. However, this margin has been narrowing, and in 2008/09, the authority made a deficit on the Collection Fund of £0.8m, of which the Council's share is just under £0.6m.

Provision has been made in setting the Council Tax for 2009/10 for a deficit, and in fact the actual deficit was less than had been predicted at the time budget decisions were made. It is too early to say what the Collection Fund position for 2009/10 will be, and if there is a further deficit, this will need to be taken into account in setting budgets for 2010/11. The Collection Fund will be kept under review and further advice provided to Members at the appropriate time.

4.13.2 Decent Homes

In July 2008, the Council established its ALMO, Tower Hamlet Homes, with a view to completing the policy to deliver Decent Homes. The ALMO procures a range of support services and its office accommodation from the Council, but has the ability as a separate Company to go elsewhere for these services if this secures better value for money for housing services. This is likely to have the impact of reducing the extent to which services within the General Fund can recharge costs to the Housing Revenue Account (HRA).

The consequence of this is that corporate and support services currently charged to the Housing Revenue Account (HRA) may need to downsize over the next few years. The impact of this on the General Fund is subject to the speed of progress. In response to this, the authority has been setting aside resources into a Housing Choice Reserve for a number of years. The reserve was reviewed in setting the budget for 2009/10 and around £15m was released to contribute towards capital spending on the Overcrowding Strategy. The balance of around £8.5m is required to manage any necessary downsizing.

It should be noted, however, that no other budget provision has been made for these costs, and any support service costs which revert to the General Fund as a results of decisions taken by Tower Hamlets Homes, and which cannot be saved, will need to be provided within future budgets, adding to the savings target for the General Fund.

4.13.3 Local Authority Business Growth Incentives (LABGI)

The LABGI allows local authorities to retain part of the growth in revenue from business rates provided that it exceeds a specified level, determined on the basis of recent historic trends. At the moment, in view of the economic downturn, no assumption of further funding from this source has been made.

4.14 Reserves

4.14.1. General Fund Reserves stand at £27.1m as at 31st March 2009. This is slightly higher than the Council's historic guide range of 5.0-7.5%. .

4.14.2. There are, however, a number of potential calls on reserves and a number of potential additions over the next few months and the projected position on reserves as at 31st March 2010 is set out at **Appendix E**. and will remain under review throughout the budget process.

5. REVISED MEDIUM TERM PLAN FOR 2010/11-2012/13

5.1. **Appendix F** sets out a revised forecast for 2009/10 to 2010/11 which brings into consideration the issues set out above relating to inflation, committed growth and the Collection Fund. All projections are based on an assumption of a 2.5% increase in Council Tax each year, although this is planning figure and not an approved target.

5.2. The principle difference between the revised Medium Term Plan and that agreed by Members in February/March is a more pessimistic Formula Grant forecast (see Section 4.7.4 above). However there are also risks associated with the current budget which are discussed above, but which are not directly reflected in this forecast and among these are;

- Loss of Housing Benefits Subsidy for homelessness
- The impact on the General Fund of delivering decent Homes
- Risks to the delivery of savings in office accommodation
- The potential loss of Specific Grants

5.3. The forecast suggests that, based on current projections, and an assessment of risk, and influenced by Members views as to an acceptable level a Council Tax for 2010/11 and/or the necessity to reprioritise expenditure, an additional savings target of between £3.0m- £4.0m would be prudent in 2010/11.

5.4. It should be noted that on the basis of the medium term forecast a minimum savings target of £27m for the period 2010/11-2012/13 is required and officers have been working to identify ways of meeting this target which will minimise the risk of reductions in services over the period of the Medium Term Plan and set balanced budgets in the next three year budget period.

6. CAPITAL PROGRAMME

6.1 Integrated Revenue and Capital Planning

6.1.1. The next section of this report sets out the outlook for Capital resources for the period 2110/11 to 2012/13.

6.1.2. Expenditure on services comprises a recurring, revenue element (eg. staff salaries, running costs, contract payments etc) and planned capital investment in assets and infrastructure (e.g. buildings, vehicles etc). Effective service delivery requires these resource elements to be considered together. The Capital Programme is concerned with planning for investment in assets and infrastructure necessary to deliver high quality services to residents.

6.1.3. The Capital Programme agreed by the Council invariably has revenue cost implications.

- Capital financing may be charged to revenue accounts either in the form of direct contributions to capital expenditure, or as costs of borrowing or other credit arrangements to finance capital expenditure.

- Building schemes normally carry with them ongoing running costs which in some circumstances cannot be met from existing resources.

It is therefore not possible to consider the Capital Programme and revenue plans in isolation from each other.

6.2. Tower Hamlets Capital Programme is divided into two elements;

- Mainstream Programme- which is funded largely from resources allocated by the Government and other funding bodies, and which follows the priorities of those funding bodies, although often with a high level of congruence with local priorities.

- Local Priorities Programme- which is funded from resources generated by the authority itself, from capital receipts, revenue contributions to capital budgets and prudential borrowing, and is allocated to the Council's own priorities.

Issues for the Mainstream Programme

6.3. Government support to the capital programme is subject to annual announcements of funding. Indications are that capital budgets will be under similar pressure to revenue allocations, and this is likely to impact upon the resources available for mainstream programmes. Theoretically, some of the funding allocated by Government is available to be spent on the Council's own priorities. However, it is thought that if Councils decided to allocate this money to areas other than those indicated, Government departments might be loathe to allocate capital resources to those authorities in future. The authority's past practice has therefore been to allocate mainstream resources to the services for which they were intended.

6.4. Some Government funding is allocated in the form of supported borrowing. In previous years, this has resulted in the allocation of additional Formula Grant to fund the borrowing cost. The fact that Tower Hamlets is now at the grant floor, however, means that it will not receive additional funding for supported borrowing. When it comes to setting the capital programme for future years, Members will need to consider whether the authority can afford to borrow this money. In the meantime, General Fund revenue forecasts assume a provision for the estimated cost of supported borrowing.

Local Priorities Programme

6.5. The level of the capital programme is being sustained in 2009/10 largely through the planned realisation of major capital receipts and the use of reserves, but this approach cannot be relied upon in future years and carries a degree of risk.

6.6. Capital receipts have largely been allocated to fund the approved Local Priorities Programme for 2009/10 and the Blackwall Reach scheme. An amount of £0.574m remains anticipated in the current year from the sale of the former Bishop Challoner school in Christian Street and there may be further income from sale of Council house, albeit that the market is currently depressed. Any further funding relies upon further asset sales which have yet to be approved by Cabinet.

In relation to the £0.574m known to be available for 2010/11, most of this is likely to be required to meet the Council's contribution to Mandatory Disabled Facilities Grants in 2010/11 for which the provisional allocation of grant from the Government indicates a Council contribution of £0.412m.

6.7. Further funding may be available in receipts over the next three years from asset sales listed in the approved Asset Management Plan. This includes Right to Buy income from the sale of Council houses, and the disposal of further sites which have been identified in the Asset Management Plan but have not yet been formally sanctioned by Cabinet. Right to Buy receipts are assumed to continue at recent levels, although there are signs that this is being impacted by the current slow down in housing markets. Further capital receipts are contingent upon other decisions and successful .

Other Potential Sources of Funding

6.8 Prudential Borrowing

The Council is empowered to set its own level of borrowing and other credit arrangements to fund capital expenditure, providing that level is affordable, sustainable and prudent. The benefit of prudential borrowing is that it enables an authority to come to its own view as to the appropriate balance between revenue and capital spending, to undertake options appraisal for revenue-intensive and capital-intensive options on a consistent basis, and to borrow for capital purposes as needs arise instead of when Government gives its approval. The Council may decide to fund additional capital expenditure through prudential borrowing where the tests of affordability, sustainability and prudence are met, and where it appears to offer value for money to do so.

Prudential borrowing is only affordable if borrowing costs can be met from revenue funding in the long term. In view of the funding gap identified in the revenue forecast, prudential borrowing should therefore be restricted to invest to save schemes where ongoing savings are at least sufficient to fund borrowing costs.

6.9 Revenue Contributions to Capital Expenditure

The opportunity to use revenue funding in this way is clearly dependent upon the availability of revenue funding. The financial outlook for General Fund presented in this report suggests that some one-off funding from LPSA Reward Grant and WNF is available in revenue budgets in the earlier years of the three year budget for capital investment if Members so choose. However, it will important to ensure that this is not invested in schemes which have substantial ongoing revenue implications which will be difficult to fund.

6.10 Impact of the Capital Programme on Revenue Budgets

In developing a strategy for the capital programme, the link between capital and revenue budgets is of key significance. There has always been such a link because of;

- the revenue implications of the capital programme- running costs and borrowing costs.
- the funding of elements of the capital programme directly from revenue budgets.
- the trade-off between routine maintenance (which should normally be funded from revenue) and structural maintenance and renovation (capital).

7. HOUSING REVENUE ACCOUNT

7.1. Traditionally in Tower Hamlets, the Housing Revenue Account has been subject to a parallel but separate budget process. However, as resources become scarcer, there is a need to ensure that the implications of spending decisions are picked up in both the General Fund and HRA and that optimum advantage can be taken of such flexibility as exists between the HRA and the General Fund to meet the Council's priorities.

7.2. There is a close relationship between the General Fund and the HRA in that;

- the General Fund provides a range of support services to the housing management functions of the Council (as described elsewhere in this report)
- because of the way the capital financing and housing subsidy system in local government works, any borrowing decisions taken by the Council to fund capital expenditure can have an impact on both the General Fund and HRA

7.3. It is therefore proposed that the budget process for the General Fund and the HRA needs to be a single process for 2010/11.

7.4. The HRA is a statutorily ring-fenced account and expenditure must relate solely to the Council's landlord functions. Its turnover is currently some £97m. To maintain a balanced HRA, costs must be contained within the income generated from tenants rents (the majority of which is supported through housing benefit), non-dwelling rents, tenants and leaseholders (and freeholders) service charges. The Council is however also one of the small minority of authorities still in receipt of HRA Subsidy. A forecast Medium Term Financial Plan for the HRA is attached at **Appendix G.**

7.5. There are a number of factors bearing on the budget process for the HRA in the period 2010/11-2012/13.

- To achieve 2* status Tower Hamlets Homes must demonstrate delivery of value for money. Failure to do this will mean that the Council does not achieve access to up to £250m of additional capital investment for Decent Homes. Audit Commission data suggest the Council and its ALMO are in the highest spending quartile for housing management.

- A Government review of the Housing Subsidy system is currently underway and is expected to take effect from 2011/12. As one of the few authorities still in receipt of positive subsidy, this is a concern to the authority and it is thought that the loss of subsidy could be as high as £9m. There is a high risk that the new housing finance system will address this perceived anomaly in the system.

- Leaseholders have questioned the high charges they receive from the Council and challenged the value for money the Council delivers in this area. The Council has committed to tackle this issue with leaseholder groups.

7.6. The forecast at **Appendix G** suggests that the HRA will have a deficit and therefore an annual savings target of £9.1m by 2012/13, representing nearly 10% of turnover. However, since around one third of the turnover of the HRA relates to capital financing costs arising from past spending decisions, and is therefore not manageable in the short term, this probably translates to around 20% of manageable expenditure. This is a similar proportion to the savings target for the General Fund over the same period.

7.7. Members need to bear in mind their priorities in relation to the Council's housing management service and consider the HRA as part of their budget strategy for 2010/11.

8. SERVICE AND FINANCIAL PLANNING 2010 TO 2013 – PLANNING PARAMETERS AND OUTLINE PROCESS

Outlook Summary

8.1. The report sets out that there are some additional growth pressures and risks relating to the General Fund for 2010/11, and although officers are seeking to take mitigating actions, the safest course at this stage is to assume that an additional savings target will be required of between £2.0m-£2.5m. However, Members may wish to seek a higher target in order to provide policy flexibility around the budget for 2010/11.

8.2. In general, funding available for capital investment in the form of capital receipts is very limited. However, there are funds available for one-off investments in revenue or capital schemes of up to £9.192m from the LPSA Reward Grant, Parking Control Account surpluses and Working Neighbourhoods Fund grant. Some of this (£2.348m) is only available for capital purposes.

8.3. The position on the HRA is that a savings target of just under £500,000 will be required for 2010/11.

8.4. Looking further ahead, resources for both the General Fund and the HRA are likely to become tighter in current economic conditions and as a result of distributional changes. Officers are planning for this eventuality.

Recommended Parameters

8.5. It is recommended that, as a minimum, Members request officers to;

- Seek General Fund savings up to a target of £2.5m, with an additional target if Members wish to provide greater flexibility over policy setting.

- Seek HRA savings of £500k, with an additional target if Members wish to provide greater flexibility over policy setting.

- Identify budget priorities for one-off capital or revenue proposals for 2010/11 and ask officers to develop proposals for consideration later in the budget process.

9. NEXT STEPS

9.1 **Budget Timetable**

A timetable for the remaining stages of the budget process is shown at **Appendix H**.

9.2 **Instructions to Officers**

Following this meeting, the Corporate Director of Resources will issue instructions to officers to seek options for delivering the budget approach agreed by the Cabinet in accordance with the timetable.

10. COMMENTS OF THE CHIEF FINANCIAL OFFICER

10.1 The comments of the Chief Financial Officer are the subject of this report.

11. RISK MANAGEMENT IMPLICATIONS

11.1 The absence of a forward financial forecast would expose the Council to the risk of making decisions which are not sustainable in the longer term, or of missing opportunities which might only be identified through a longer term planning horizon. Furthermore, inadequate integration of service and financial planning gives rise to the possibility of service planning without regard to affordability, or a budget that does not direct resources to service priorities.

11.2 This report, and its subsequent development, is intended to substantially address those risks.

11.3 The timetable includes provision to consider specific financial risks as part of the budget making process, initially in the Autumn. The Director of Resources will report further to Members throughout the budget process.

12. EFFICIENCY STATEMENT

12.1 Local Government is required to achieve a 3.0% efficiency target in 2008/09 and for each of the next two years. However, no target has been set for each individual authority and the priority for budget planning over the period which is the subject of this report will be to set balanced budgets which meet Council priorities.

12.2. The efficiency and value for money implications of individual budget proposals will be set out as part of the budget process as it progresses.

13. CONCURRENT REPORT OF THE CHIEF LEGAL OFFICER

13.1. The report provides Cabinet with information concerning the current financial outlook, the budget process and the housing revenue account. Cabinet is asked to determine a budget strategy and agree a budget process.

13.2. The setting of the budget falls to the Full Council under the Council's Constitution. The Council is required pursuant to section 151 of the Local Government Act 1972 to make arrangements for the proper administration of its financial affairs. The chief finance officer is responsible for that administration. It is proper for the chief finance officer to bring forward the information in the report to Cabinet, for Cabinet to determine a strategy for preparation of the budget and for Cabinet to agree a budget process.

14. ONE TOWER HAMLETS CONSIDERATIONS

14.1. The budget and Medium Term Financial Plan is one of the main instruments through which the Council delivers its Strategic Plan, including its objective to promote One Tower Hamlets. It is important that decisions taken as part of the budget process take account of equalities and diversity issues.

15. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

15.1 SAGE considerations have been taken into account in the forecasts.

16. INDEX OF APPENDICES

Appendix	Detailing the following:
A	Medium Term Financial Plan 2009/10 – 2011/12
B1	Committed Growth – agreed for 2009/10 – 2011/12
B2	Committed Growth – due diligence
C1	Savings – agreed for 2009/10 – 2010/11
C2	Savings – due diligence
D	Service Improvement Growth – agreed for 2010/11
E	General Fund Balances
F	Revised Medium Term Financial Plan 2009/10 – 2010/11
G	HRA – Medium Term Financial Strategy
H	Budget Timetable

LOCAL GOVERNMENT ACT 1972 (SECTION 100D)
LIST OF "BACKGROUND PAPERS" USED IN THE PREPARATION OF THIS REPORT

Brief description of "background papers"	Tick if copy supplied for register	If not supplied, name and telephone number of holder
Held by Resources Directorate 5th floor, Mulberry Place)		Alan Finch 020-7364-4915