

Committee/Meeting: Overview & Scrutiny Committee Cabinet	Date: 8 th February 2011 9 th February 2011	Classification: Unrestricted	Report No:
Report of: Corporate Director – Resources Originating officer(s): Chris Naylor, Corporate Director-Resources & Alan Finch, Service Head – Corporate Finance		Title: General Fund Revenue Budget and Medium Term Financial Plan 2011/2012- 2013/2014 Wards Affected: All	

Lead Member	Cllr Alibor Choudhury, Lead Member Resources
Community Plan Theme	One Tower Hamlets
Strategic Priority	All

1. SUMMARY

- 1.1. This report invites the Cabinet to submit its recommendation for the General Fund budget and Council Tax for 2011/12, and a Medium Term Financial Plan 2011/12- 2013/14 to Budget Council for consideration on 23rd February 2011.
- 1.2. On the 12th January, the Cabinet considered the General Fund revenue budget and referred initial budget proposals to Overview & Scrutiny Committee for consultation in accordance with the Budget & Policy Framework.
- 1.3. The Overview and Scrutiny Committee was due to meet to consider these matters last night (8th February) and any comments will be reported to your meeting this evening. This report also sets out the results of public consultation on the budget, with residents and business ratepayers.
- 1.4. At the time of submitting this report, the Government had not yet announced the Council's final Formula Grant settlement for 2011/12. There is not expected to be any change from the provisional figure announced in December. A further report will be made at your meeting if necessary.
- 1.5. The Greater London Authority (GLA) is meeting to sets its precept on 23rd February, and the report sets out the latest available information on the Mayor's budget proposals at the time of writing and any update will be

provided verbally at your meeting. The final GLA budget and precept will be reported to Council on 23rd February.

- 1.6 This report also includes final advice from the Corporate Director of Resources on the financial risks facing the authority and his statutory advice on the robustness of the budget process. The report considers the impact of risk on the overall General Fund budget, and reviews the level and planned use of general and earmarked reserves. Cabinet is asked to consider a strategy in relation to maintaining reserves at a level consistent with known pressures on the Council's budget and unquantifiable future risk.
- 1.7. Four other reports on this agenda are also concerned with budgeting and forward financial planning for the next three year period and each will impact upon the General Fund. Appropriate cross-references are included in this report. These are;
- Housing Revenue Account budget 2011/12-2013/14
 - Dedicated Schools Grant Allocation 2011/12
 - Capital Programme 2011/12-2013/14.
 - The Council's Treasury Management Strategy and Prudential Indicators for 2011/12, which is concerned with the management of the Council's borrowing and investments for the next financial year and with setting affordable limits for borrowing and capital expenditure.

2. DECISIONS REQUIRED

The Overview & Scrutiny Committee is recommended to consider the report and recommendations and pass any comments it may have to the Cabinet for consideration at its meeting on 9th February 2011.

The **Cabinet** is recommended to:-

Budget Consultation

- 2.1 Consider any comments or recommendations of the Overview and Scrutiny Committee.
- 2.2 Consider the outcome of the various consultations carried out in relation to this budget as set out in **Appendix H (to follow)** and Section 6.

Grant Funding

- 2.3. Note the funding available for 2011/12 and the indications and forecasts for future years (section 8);

Directorate Base Budgets 2011/12

- 2.4 Approve the base budgets for 2011/12 for each Directorate as set out at **Appendix A.**

Approved Budget 2010/11

- 2.5 Agree the growth contingency and savings for 2011/12 as set out in Sections 10, 11 and 13 and **Appendices B and D** and note the implications for later financial years.

Medium Term Financial Plan 2011/12-2013/14

- 2.6. Note the Medium Term Financial Plan set out at **Appendix C,** the savings target arising in relation to future years and the actions being undertaken to address it.

Financial Risks: Reserves & Contingencies

- 2.6 Note the advice on strategic budget risks as set out in section 15 and **Appendix E,** in particular the significant increase in risk that the Council is exposed to as a result of the financial settlement, and the proposed response of the Council to managing this risk.

Robustness of the Budget Process

- 2.9. Note the advice of the Corporate Director- Resources in relation to the robustness of the budget process as set out at Section 17.

Balances/Reserves

- 2.7 Note the review of reserves as set out in section 16 and further detailed in **Appendices F and G.**
- 2.8 Note officers' advice on the strategy for general reserves and note that this will be further considered by the Cabinet in February.

General Fund Revenue Budget 2011/12

- 2.9 Agree a General Fund Revenue Budget of £310.960m and a Council Tax (Band D) of £885.52 for 2011/12 and refer the proposal to Budget Council for consideration.

3. REASONS FOR THE DECISIONS

- 3.1 The Council is under an obligation to set a balanced budget for the forthcoming year and to set a Council Tax for the next financial year by 10th March 2011. The setting of the budget is a decision reserved for Council.
- 3.2 The announcements that have been made about Government funding for the authority require a robust and timely response to enable a balanced budget to be set.

4. ALTERNATIVE OPTIONS

- 4.1 The authority is bound to respond to the unprecedented cuts to Government funding of local authorities and to set an affordable Council Tax and a balanced budget, while meeting its duties to provide local services. This limits the options available to Members. Nevertheless, the authority can determine its priorities in terms of the services it seeks to preserve and protect where possible, and to a limited extent the services it aims to improve further during the period of cuts.

5. BACKGROUND

- 5.1. At its meeting on 12th January, the Cabinet received a report setting out budget proposals for 2011/12-2013/14. These proposals were the result of a lengthy planning process. Cabinet confirmed the base budget for 2011/12, considered growth pressures and risks bearing on the Council's budget and agreed initial proposals for efficiency savings to address the funding cuts announced by the Government in December.
- 5.2. This report invites the Cabinet to set its final proposal for the General Fund Revenue Budget and Council Tax for 2011/12 and medium term financial plan to the end of 2013/14 and refer these for approval to Budget Council on 23rd February 2011.
- 5.3. This report should be considered in conjunction with the reports on the Capital Programme and the Housing Revenue Account, which are also on this agenda, and the Council's Strategic Plan. Together these reports ask Cabinet to consider a number of key strategic issues and to make decisions that will enable next year's budget to be formulated.
- 5.4. The budget proposals have been considered as part of a strategic & resource planning framework, which identifies how budget proposals contribute to the delivery of the Strategic Plan and Community Plan. In considering officers' proposals, leading Members have regarded them in the context of;

* the strategic direction for services,

- * the need to identify a medium term efficiency programme that takes account of the need to deliver the magnitude of savings required to balance the medium term financial plan.
- * the relative costs and performance of existing services, and
- * budget planning which is at the heart of the Council's overall planning process.

- 5.5. In formulating its budget proposal, the Cabinet needs to consider the decisions made to date alongside the advice of officers on budget pressures and risk, consider contributions to budget contingencies, reserves and balances, and in so doing establish a balanced and robust budget for 2011/12 and a sustainable medium term financial strategy for the Council.
- 5.6 Budget decisions taken in setting the budget for any one financial year have an impact well into the future. In this context, the three year balanced budget strategy and maintenance of a Medium Term Financial Plan puts the Council in a strong position when making budgetary judgments in 2011/12.
- 5.7. The Government Spending Review announcement on 20th October confirmed that local government is facing probably the deepest and most sustained cuts in Government funding for many decades. In setting a budget for 2011/12, it is essential that Members have regard to the financial projections and risks set out in this report and in the Medium Term Financial Plan.

6. BUDGET CONSULTATION

- 6.1. Formal budget consultation is taking a number of forms:-
- Consultation with the Overview and Scrutiny Committee under the Council's Budget and Policy Framework.
 - Statutory consultation with the business community;
 - Budget Congress meetings with partners and community representatives.
 - Public consultation through a number of focus groups over the consultation period.

Responses to Consultation

- 6.2. The Overview & Scrutiny Committee was due to consider the Cabinet's initial budget proposals at its meeting yesterday (8th February), after the preparation of this report. Any comments or recommendations made by Overview & Scrutiny Committee will be reported to you at this evening's meeting.
- 6.3. The results of public consultation are set out at **Appendix H [to follow]**

- 6.4. The results of statutory consultation with the business community are not to hand at the time of preparing this report and will be reported at your meeting.
- 6.5 Cabinet should consider the results of these consultations in allocating resources and recommending the total budget requirement and Council Tax for 2011/12

7. PROJECTED OUTTURN 2010/2011

- 7.1. The projected outturn for the Council's General Fund for 2010/11 is currently £311.153m, which represents a projected overspend against service budgets of £1.084m. The over spend is a matter of concern, and it reflects growth pressures arising in 2010/11, which are discussed in relation to 2011/12 budget pressures below.

8. FUNDING FOR 2011/12 and LATER YEARS

Formula Grant

- 8.1. At the time of submitting this report, the Secretary of State for Communities and Local Government had not announced the final local government finance settlement for 2011/12. However in recent years these have always done no more than confirm the figure provided for consultation and the same is expected this year. A further report will be made at the meeting if there is any change in this position.
- 8.2. The Formula Grant comprises;
- A 'Relative Needs Amount' (RNA) which allocates resources in accordance with the needs of the authority relative to others. Tower Hamlets continues to have one of the highest relative needs allocations in the country.
 - A 'Relative Resource Amount' which allocates resources in accordance with relative Council Tax base per head of population. This provides for the partial equalisation of resources between those authorities with a high tax base and those with a relatively low tax base. Once again, Tower Hamlets receives a relatively high allocation in this block.
 - A 'Central Allocation' which is a standard amount per head of population and does not vary significantly between authorities.
 - A 'Floor Damping' amount which, for Tower Hamlets, supplements the amount of Formula Grant to be received to the level of the minimum guaranteed increase, or floor.

In addition, for 2011/12 and 2012/13, the grant includes an adjustment relating to a number of former specific grants transferred into Formula Grant which increases the baseline for the Formula Grant by £26.7m. This incorporates a

baseline adjustment which assumes the authority's central education costs will be reduced by about £1m as a result of the setting up of Academies, despite the fact that there are no Academies in Tower Hamlets.

8.3. Tower Hamlets' provisional allocations for the two years are;

<u>Table 8.3 Formula Grant Provisional Settlement 2011/12 and 2012/13</u>	Formula Grant (adjusted) 2010/11 £m	Formula Grant 2011/12 £m	Provisional Formula Grant 2012/13
Block			
Relative Needs Amount	212.847	201.410	177.224
Relative Resource Amount	(32.613)	(33.512)	(33.167)
Central Allocation	44.097	32.841	29.598
Floor Damping	7.872	6.336	15.679
Adjustment for former specific grants transferring into Formula Grant	26.728	22.597	22.500
Formula Grant	258.932	229.673	211.835
Change on previous year (Grant floor increase)		-11.3%	-7.8%

Thus Tower Hamlets' Formula Grant will reduce by £47.1m (18.2%) over the two years 2011/12 – 2012/13.

8.4. The Formula Grant was subject to a review of distribution for 2011/12 and the Council raised three issues in particular with the Government under the consultation. The outcome was;

- Against the authority's wishes, the Government has adopted proposals that reduce the weighting given to labour costs in the Area Cost Adjustment. On a like for like basis this has probably cost the authority about £6.7m a year against its undamped grant settlement.
- Against the authority's advice, the Government has removed Bangladeshi children from the definition of low achieving ethnic groups. This probably costs the authority £1.3m in undamped Formula Grant, although there is a concern that the adjustment may in time also be made to schools grants with a much greater effect.

- The impact of these changes has, however, been damped by the Government through a series of banded grant floors, ranging from -11.3% to -14.3% in 2011/12. Tower Hamlets has successfully lobbied for fair treatment through the damping mechanism. Tower Hamlets is in the highest of these bands, which gives it a final damped settlement of -11.3%. This is lower than the average -9.9% settlement for England but higher than the average -11.6% settlement for authorities with a similar range of responsibilities. However it also needs to be recognised that damping is only temporary and is ultimately not a substitute for a fair settlement.
- 8.5. There is as yet no announcement of funding beyond 2012/13 pending a full review of Local Government finance that the Government intends to undertake during 2011. For Medium Term Financial Planning purposes, the national figures announced in the Spending Review have been used.
- 8.6. Tower Hamlets is also one of three authorities in London which are in receipt of a Transitional Grant in 2011/12 (Hackney and Newham are the others). This has been calculated to ensure that no authority's 'revenue spending power' reduces by more than 8.9% across all funding streams, including Council Tax, Formula Grant and specific grants. Tower Hamlets will receive £3.767m in 2011/12, but this will discontinue for 2012/13. This has the effect of softening the front-end loading of the settlement slightly by moving some of the three-year savings target back to 2012/13, but it does not change the extent to which the Council's total budget will need to reduce over the two years 2011/12 and 2012/13.

Specific Grants

- 8.7. Generally speaking, the Government has adopted a policy of removing ringfencing and reducing the number of specific grants. This makes for a simpler settlement and provides authorities with greater financial flexibility than they might otherwise have had, although this has to be seen in the context of funding reducing substantially in cash terms.
- 8.8. The Area Based Grant introduced in 2008/09 has been discontinued, and much of the funding allocated through it has been employed through Dedicated Schools Grant and a new Education-related grant called the Early Intervention Grant. As a result of grant transfers involving the main non-ringfenced grants of Formula Grant and ABG, there is a net reduction in such grants previously allocated to fund Council expenditure of £4.802m and this is reflected in the Council's savings target for 2011/12.
- 8.9. The following specific grants were also announced as part of the draft settlement and it is thought that there will be only eight specific grants allocated by the Government in 2011/12

Table 8.9 Specific Grants	8.9 Specific Grants 2011/12	2010/11 Actual	2011/12 Provisional	2012/13 Provisional	Status
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2012/13	£m	£m	£m	
Dedicated Schools Grant & Pupil Premium	289.778	302.849	Not announced	Ringfenced
Early Intervention Grant	N/A (*)	20.383	20.757	Non-ringfenced
Learning Disabilities & Health Reform Grant	N/A	1.774	1.816	Ringfenced
Preventing Homelessness Grant	0.880	1.925	1.925	Non-ringfenced
Housing & Council Tax Benefits Subsidy Admin Grant	4.667	4.662	Not announced	Non-ringfenced

(*) The grant has been funded by discontinuing various other former grants

Children's Services

8.10. The grants position affecting Children, Schools and Families is complex. A report concerning the allocation of Dedicated Schools Grant (DSG) appears elsewhere on the Cabinet's agenda for this evening. The Government has abolished a large number of former funding streams, some of which have been brought within the DSG, and has created a Pupil Premium. The DSG report sets out the implications of this in detail. The authority is limited to a maximum amount of DSG funding which can be set aside to fund central expenditure (the Central Expenditure Limit) and in order to remain within this target, a combination of measures is set out in the DSG report including delegating additional funding to schools and some cost savings. There will be costs of implementing these savings estimated which cannot be charged to the DSG and will need to be met from reserves and contingencies within the General Fund. Since some of the implications are dependent upon decisions by individual school governing bodies, the full impact cannot be estimated at this stage, but it is thought that costs of implementation will not be less than £1m.

8.11 The Government has also created a single large specific grant for Education called the Early Intervention Grant which has been formed by drawing together a number of other former specific grants including some ABG. Although this grant is non-ringfenced, the size of the grant and the fact that the former grants used to create it comprise a large proportion of the funding for the non-schools Education budget means that the only possible decision is to allocate the grant for children's services use. The allocation for 2011/12 is £20.383m which compares with £23.546m which the authority has budgeted to spend against these grants in 2010/11. Further savings will therefore be necessary to enable the Directorate to remain within the available funding and the Director will devise a separate set of proposals for the Cabinet to consider at a future meeting.. However, to allow a meaningful dialogue with schools

about these budgets and to allow time for uncertainty about two additional grants (Youth Justice Board and Music Grant) to be resolved, it is proposed that any savings required should be implemented for the new school year in September 2011. The cost of this can be covered from contingencies.

- 8.12. The risk that schools may choose not to buy-back a greater range of services is one that will take some time to clarify, because individual schools will need to make decisions about individual services, which will then feed through to the income generated from schools for those services, possibly in a gradual way. This is also likely to be a permanent risk for some services because even if schools choose to buy back at this stage, they will be able to make different decisions in the future. The Council's reserves and contingencies policy will need to take this into account.
- 8.13 Announcements are awaited in relation to one other significant grant, the Lifelong Learning Grant from the Skills Funding Agency, which provides the Council with £2.812m in the current financial year. An announcement is anticipated, although the amount is not known and this funding stream must also be considered as a risk.
- 8.14. The Government has announced that additional funding to support social care will be paid to the authority via the NHS, and a provisional figure of £3.725m has been published. However the terms for the allocation of this funding are not known, although the Government says it expects local authorities and the NHS to work together on how the money should best be spent. Elsewhere in this report, a number of risks relating to cost pressures are set out including some relating to Social Care, and it may be that this additional funding can be applied to strategies which will manage that risk while avoiding cost transfer to other agencies such as hospitals. It is suggested that this funding should be held against those risks at this stage.

Ministerial Statement in relation to Council Tax

- 8.15. In his provisional settlement statement, the Secretary of State confirmed that he intends to replace the current capping power with a power for residents to veto excessive Council Tax increases through a referendum. However this will require primary legislation and in the meantime current capping legislation remains in place. The Secretary of State gave a strong indication that capping powers would be used on any authority that proposes an increase in Council Tax deemed to be excessive.
- 8.16. Section 18 of the report discusses Council Tax further.
- 8.17. Cabinet is asked to note the details and impact of the local government finance settlement and other grant allocations for 2011/12 and 2012/13.

9. PROVISIONAL BUDGET TARGETS 2011/2012

- 9.1. Budget decisions for 2011/12 will be based upon a provisional budget target, the starting point for which is the original approved budget for 2010/11 of £310.369m.
- 9.2. At Cabinet in July, Members agreed a package of savings in response to in-year cuts in funding imposed by the Government at its Emergency Budget in May. In consequence of this, the detailed allocation of the current budget differs from the original budget for 2010/11 approved in March. **Appendix B** sets out how the 2011/12 base budget differs from the original approved budget and shows the base budgets for 2011/12 for each Directorate which, subject to adjustments for savings, Corporate Directors will be expected to manage within over the next financial year.
- 9.3. Asset Rentals and Support Service Charges will be adjusted for, subsequent to this meeting. However, the impact on the General Fund budget is neutral.

10. COMMITTED GROWTH 2011/2012- 2013/2014

- 10.1 Committed growth is additional spending that, for all practical purposes, is unavoidable. It includes new statutory requirements, responsibilities transferred from the Government and other bodies, new taxes and demand led growth (which arises when there is an increase in the number of clients requiring statutory services).
- 10.2 All bids for committed growth have been reviewed collectively by the Chief Executive and Corporate Directors and the following working definition has been applied:-

“Where the Council has discretion over whether it incurs the expenditure, then this should not be regarded as committed growth, regardless of the impact on service performance.”

A number of items have come forward which, for various reasons, it is not possible to contain within existing plans and these are detailed at **Appendix C.** These have been considered by Corporate Management Team and the Mayor and none of them currently fully meet the definition of committed growth, although they are risks to the Council’s budget. The growth risks listed at Appendix B total £7.433m but officers are confident that these can be managed down by between 25%-30% in 2011/12 and a growth contingency of £5.5m is therefore recommended.

- 10.3. Committed Growth forecast for 2012/13 and other future years will be subject to review and further scrutiny in subsequent budget rounds. For the purposes of the Medium Term Financial Plan, it represents a planning figure and not an allocation of funding to the Directorate in question.
- 10.4. **Capital Financing & Investments**

The cost of past borrowing, less the income from investments, must be provided for within the budget. The calculated impact of this, based on a forecast of interest rates, is as follows;

Table 10.4	2011/12 £000s	2012/13 £000s	2013/14 £000s
Capital Financing & Investments	777	-50	84

10.5. Pensions Fund

The Council's Pension Fund is subject to a triennial revaluation of its assets and liabilities. This year's revaluation has taken place at the of a three year period in which investment performance has been seriously affected by the credit crunch and the recession that followed. Liabilities to the fund continue to rise as a result of increased longevity. Following discussion with the actuary it is necessary for the Council to increase its contributions to the Fund.

Table 10.5	2011/12 £000s	2012/13 £000s	2013/14 £000s
Pensions Fund	900	2,150	3,400

The Hutton Commission into public service pensions is expected to report in 2011 and is likely to recommend measures to rebalance the future costs of the scheme between taxpayers and beneficiaries in favour of the taxpayer. The implications of this would first be felt in the 2013 revaluation. The impact of this is not known and therefore it is not reflected in the actuarial revaluation.

11. INFLATION & OTHER CONTINGENCIES

- 11.1. The authority's budget needs to include financial provision for inflation and for other risks and uncertainties, especially those which are outside the Council's control.

Inflation

- 11.2. The impact of inflation on the costs of providing Council services is effectively unavoidable; The Council is negotiating with existing suppliers over prices as part of its response to Government cuts, but in general if prices on offer to the Council rise in line with inflation the Council is obliged to pay them.
- 11.3. There was no Local Government pay award in 2010 and in June, the Chancellor of the Exchequer called for a further two year pay freeze for all public sector workers with salaries of more than £21,000 a year, who should receive a £250 flat rate. The Trade Unions have submitted a pay claim for £250 on *all* salaries.
- 11.4. Non pay inflation in the economy has been high as the impact of quantitative easing and other factors have fed through to the money supply. The Medium Term Financial Plan provides for inflation at 2%, which is in line with the Government's long-term target but could be a low estimate. Taking pay and

non-pay factors together the inflation contingency for 2011/12 is recommended to be £4.491m. Any increase in inflation above this will need to be found from within Directorate budgets.

12. MEDIUM TERM FINANCIAL PLAN

- 12.1. The development of the 2011/12 budget has taken place within the context of a longer term strategic and resource planning process. The Government has published Spending Review figures up to the end of the current Parliament, and these show that the challenging outlook for the public finances will persist at least until 2014/15 and possibly beyond. The measures taken to balance the budget in 2011/12 will enhance the Council's financial resilience as we enter this period.
- 12.2. Whatever the constraints, it is important that resource allocation is seen in terms of the outputs and outcomes that are expected as a result of financial decision. The allocation of funding has been considered in the light of its impact on the delivery of services.
- 12.3. The fact that resources are now shrinking instead of growing as in recent years makes no difference in principle to this approach, which has designed to ensure that:-
 - A forward looking financial forecast influences the development of service plans
 - Service plans identify the financial consequences of proposed actions, including the resource implications associated with achieving the objectives set out in the Strategic Plan.
 - Financial plans allocate resources to address changing community needs and priorities.
 - Resources are directly related to performance improvement in order to minimise costs and optimise value for money.
 - Different options for delivering policy outcomes are examined and taken into account.
 - Service and financial plans address key risks to budgets and performance.
- 12.4. In addition to the funding issues described above, the Council's budget will continue to experience additional demands over the medium term from population growth. This means that in practice the reductions in grants that are publicised will be greater when expressed in terms of the budget the Council has available per head of population.
- 12.5. A detailed medium term financial projection for 2011/12-2013/14 is attached at **Appendix C** . It indicates that the financial settlement and other pressures

identified in this report will result in an estimated savings target for the Council of £29.9m in 2011/12, a further £33.0m in 2012/13 and a further £9.1m in 2013/14.. The total savings target for the 3 years is £72.0m which compares with £70.2m reported to the Cabinet in August.

- 12.6. Based on figures in the Spending Review, a provisional savings target of around £20m for 2014/15 can be assumed. 2013/14 therefore seems to be respite from the larger annual savings figures not a return to normal. The actual figures for both 2012/13 and 2013/14 will be dependent upon a number of factors, not least the Government's announced review of the local government finance system in 2011/12.
- 12.7. The transitional funding announced as part of the funding settlement has therefore slightly eased the front-end loading expected in the Spending Review, especially for high needs authorities like Tower Hamlets. However in doing so, it has simply moved some of the problem back to 2012/13. This provides some extra time for authorities to deliver on change projects, but it will not affect the total level of budget reduction required by the end of 2012/13.

13. BUDGET SAVINGS & EFFICIENCIES

- 13.1. The impact of the Spending Review on the Medium Term Financial Plan confirms a tightening financial position for the Council for 2011/12 and beyond. At the same time the Council will continue to face significant and largely unavoidable spending growth and inflation pressures.
- 13.2. Efficiency savings for 2011/12 agreed at Cabinet in July are included in the base budget as set out in **Appendix A**, £2.790m are not ongoing, in addition to which £0.239m of savings agreed in previous financial years are not ongoing into 2011/12.
- 13.3. In addition, the previously agreed HR Improvement Programme was implemented in November which results in £1.500m in savings for 2011/12 through restructuring and streamlining HR business processes. This saving counts towards the target required for 2011/12.
- 13.4. The authority has also been advised of reductions in payments to two bodies. The Audit Commission has announced a reduction in fees that should translate to a £45,000 saving for Tower Hamlets, while London Council subscriptions will reduce by £65,000 for 2011/12.
- 13.5. In accordance with the Cabinet's instructions in August, officers have identified a range of savings opportunities which will minimise the risk to service outcomes over the three year period. Offsetting savings and efficiencies identified by each directorate are shown below. A more detailed summary is included as **Appendix D1** and the detail of each saving identified by Directors which has an impact in 2010/11 is provided in **Appendix D2**.

14. CAPITAL

- 14.1 A report elsewhere on this agenda seeks approval for a draft capital programme for 2011/12-2013/14.
- 14.2 The authority's revenue budget and its capital programme are closely linked. Both the revenue budget and capital programme are designed to support the delivery of key objectives. In financial terms, there are revenue implications associated with capital investment: part of the capital programme is directly funded by the revenue budget, while any borrowing undertaken by the authority impacts on revenue through the costs of interest and debt repayment. As indicated above, the Medium Term Financial Plan includes provision for the ongoing costs of past borrowing.
- 14.3 The resources available to fund the capital programme have reduced over the last few years. Funding for the Council's own capital spending priorities (the Local Priorities Programme) is now heavily dependent upon a few large scale asset sales and receipts from this source can therefore not be relied upon. In setting the capital programme for 2011/12 and beyond, the Council will initially be restricted to sources of funding already available, including receipts from assets already disposed of or where sales have been arranged.
- 14.4 An option normally open to the Council is to provide more funding through the revenue budget, either through direct contribution or through borrowing, providing it is shown to be prudent and affordable. As this report makes clear, the very tight funding position of the Council's revenue budgets means that opportunities for funding capital from revenue budgets and reserves are very limited and the Council is not in a position to consider capital expenditure funded from revenue sources or from borrowing until it is satisfied that a balanced revenue budget position has been reached.

15. FINANCIAL RISKS: RESERVES & BALANCES

- 15.1. A robust, transparent and sustainable annual budget and medium term financial strategy requires an assessment of the financial impact of the key risks identified through the Council's risk management process, and identification of the financial mechanisms for funding those risks should they materialise.
- 15.2 The Audit Committee and the Corporate Management Team receive quarterly reports on the key strategic and corporate risks impacting on the authority. Senior Finance Officers have evaluated these risks to assess their potential financial impact and identify how they should be reflected in the Council's financial planning. Three categories of financial risk are identified:
- Where the implications would be accommodated within existing financial provisions, such as directorate budgets or earmarked reserves.
 - Where specific risk financing arrangements are in place, such as those covered by insurance.

- Those which need to be taken into account at a corporate level as part of the budget process.
- 15.3 Issues which fall into the final category include:-
- Business continuity issues, such as systems breakdowns, contractor failure or loss of a key administrative building.
 - Risks associated with large-scale projects.
 - Risks associated with the implementation of legislation and guidelines.
 - Strategic financial risks, including changes in budgetary assumptions, overspends and major financial control failures
- 15.4 **Appendix E** sets out those strategic and corporate risks (drawn from the Council's risk register) which would be likely to have a financial impact if they were to materialise, together with the key risk areas in service/Directorate budgets and associated mitigating measures.
- 15.5 There are three ways in which risks can be dealt with within the budget;
- By having regard to risks in setting levels of general balances and earmarked reserves
 - Through setting aside specific contingencies within the budget for allocation during the year as and when required (see Section 9 above).
 - By funding specific risk mitigation programmes with the aim of reducing the potential financial impact on the Council in the future.
- 15.6. These approaches can be thought of in a hierarchy:-
- General balances are used in the main to cover unknown and unforeseen eventualities.
 - Earmarked reserves are set aside for specific issues that are more likely to occur, but where the financial impact and the timing is uncertain.
 - Contingencies are used for risks that, if they arise, are almost certain to materialise during the next budget year.
 - Funding of risk mitigation measures is appropriate for large and relatively certain risks, where it can be shown that allocating funding is likely to prevent larger risks from developing later.
- 15.7 There are a number of aspects of the budget where information is still awaited or where the impact of changes is not yet sufficiently clear to provide budget certainty. A level of uncertainty and risk is inherent in any budget setting process.

16. BALANCES/RESERVES

- 16.1. Where financial risks cannot be dealt with in other ways, it is essential that the authority provides adequate financial cover in the form of reserves or balances. This includes cover for eventualities which are outside the Council's control.
- 16.2. Financial risks which can be identified to particular causes are normally dealt with through 'earmarked' reserves. Unforeseen eventualities are covered through general reserves, otherwise known as 'balances'. Reserves and balances must be set at an appropriate level, neither too low (which would put the authority at financial risk) nor too high (which would tie up resources that could be used to deliver Council priorities).
- 16.3. The consequence of setting balances too low is that unforeseen circumstances could lead to overspends which cannot be met from Council resources. In these circumstances, authorities have no option but to take rapid action to reduce costs, which can have unplanned and unwanted consequences for service delivery. It is the responsibility of an authority not just to meet the current overspend, but also to find sufficient resources to rebuild balances to an appropriate level. This is a situation which a handful of authorities find themselves in each year, despite their best efforts.

General Reserves

- 16.4. Statute requires local authorities to set a balanced budget and places responsibilities and powers with the chief finance officer (CFO) should serious problems arise (including in relation to reserves). External auditors are responsible for reviewing and reporting on financial standing but are not responsible for setting a minimum level of reserves.
- 16.5. The level and use of reserves must be determined by the Council, informed by the judgement and advice of the CFO. When calculating the budget requirement, the CFO must report to Members on the adequacy of reserves. The Secretary of State has powers if necessary to set a minimum level of reserves.
- 16.6. The Council needs to consider the level of its reserves as an integral part of its medium term financial planning. Advice set out at **Appendix F** outlines the reasons for keeping adequate reserves and some of the issues that need to be taken into account in judging whether or not reserves are adequate.
- 16.7. In outline, in order to assess the adequacy of general reserves, the strategic, operational and financial risks facing the authority need to be taken into account. Financial reserves have an important part to play in the overall management of risk in the Council. Authorities with adequate reserves and sound financial health can embark on more innovative programmes or approaches to service delivery, knowing that the Council has sufficient financial capacity to manage any associated risks.

- 16.8. There is therefore no 'correct' level of reserves, and a particular level of reserves is not a reliable guide to the Council's financial health. The Audit Commission no longer assesses reserves against a specific, numerical guideline. However the external auditor will normally comment on the adequacy of reserves in his Annual Audit Letter.
- 16.9. The Council faces an unprecedented financial challenge in an extremely uncertain environment and this carries attendant financial risks.
- * As an authority representing a relatively deprived area, the Council is highly dependent upon Government grant and therefore has a high exposure to the general tightening of the public finances. The Government has provided grant figures for 2011/12 and, in some cases, for 2012/13, but has also shown in the past that it is willing to revisit grant allocations in-year if necessary.
 - * Aspects of the economy remain very uncertain, with the main threats being inflation (which could increase the Council's costs) and a double-dip recession (which could impact the Council's costs but also lead to the Government revisiting its public spending decisions). The third quarter economic growth figures announced in January indicated that the economy shrank once more in the final months of 2010, raising the prospect of a double-dip recession. In response the Government has reaffirmed its determination to keep downward pressure on public spending.
 - * The Government has also announced a review of local government finance which it will be undertaking in 2011 and is expected to be implemented from 2013/14. We do not know what the impact of this will be, but recent reviews have tended to be disadvantageous to high needs authorities, especially those in inner city areas.
 - * Population growth in Tower Hamlets can be expected to continue, but without the increases in funding required to sustain it without substantial change management.
 - * As set out in Section 8 above, the education settlement introduces some new risks to services provided centrally by the authority on behalf of schools.
 - * The Council also has an ambitious improvement and efficiency programme, and a number of major and interdependent projects, with significant financial implications, which will come to fruition in similar timescales over the next three years. The risk of not achieving savings must be taken into account.
 - * The programme of savings will involve costs in relation to project management. In addition, there will be costs incurred in implementing proposals. For example, £4m has been set aside from reserves (with a

further £4m from contingencies) to fund staff severance packages in the current financial year.

- * The Council has made other allocations from reserves over the recent period, such as those made to fund the housing overcrowding strategy and, within the last year, an allocation of £2.5m from general reserves to deal with the renegotiation of the Schools PFI contracts in relation to Building Schools for the Future.
- * Although the Council has done well in identifying £56m worth of savings over the next three years, the total target for the same period is £72m, and potentially over £90m over the course of the next four years if Spending Review figures are borne out.

16.10. Having regard to the potential for volatility in the medium term financial outlook, the time-limited nature of the Collection Fund surplus (paragraph 17.3), and the strategic financial risks highlighted in this report, it is recommended that Cabinet seeks to maintain general reserves at between 5% and 7.5% of budget requirement. This broadly equates to a target range of £15.7m to £23.6m.

16.11. A projection of the level of general reserves anticipated as at 31st March 2011 is shown at **Appendix G** and indicates that reserves are currently expected to stand at £20.6m as at 31st March 2011, which is in the middle of the recommended range. However in view of the financial risks facing the Council over the next few years as set out in 16.9 and in more detail at **Appendix F**, in particular the need to identify further savings after 2011/12 and the delivery risk of achieving a £30m savings plan in 2011/12, it is recommended that the reserves need to be maintained at the upper end of the range. A contribution of £3.0m is therefore included as part of the budget strategy for 2011/12.

17. ROBUSTNESS OF THE BUDGET PROCESS

- 17.1. Under Section 25 of the Local Government Act 2003 it is a requirement for the chief finance officer to report on the robustness of the estimates and the budget process
- 17.2 The following table sets out the key strategic budget risks and the principal mitigating measures;

Strategic Budget Risk	Principal Mitigating Measures
The allocation of resources does not reflect the Council's priorities as set out in the Strategic Plan.	The Council's budget and service planning processes are aligned. Financial plans are developed concurrently with service plans and reviewed against information on performance and inspection; cost, procurement and value for money; user consultation and feedback; and policy developments and other pressures for change. Annual budget decisions are set in the context of a longer

	<p>term financial outlook which identifies the resource implications of achieving the objectives set out in the Strategic Plan.</p> <p>The revenue and capital budget processes are conducted concurrently, and cross-referenced, to ensure that the Council's priorities are addressed in the most appropriate way.</p> <p>All growth and savings options are evaluated for their impact on the Council's key priorities and the Tower Hamlets Index.</p>
<p>Resource and spending projections prove over-optimistic or otherwise inaccurate</p>	<p>Savings targets are set to achieve a balanced budget in the event of a realistic settlement scenario. Reserves and balances are maintained to ensure that a worst case scenario can be managed. Budget assumptions are subjected to sensitivity analysis to ensure the risks are recognised. Committed growth bids are challenged to ensure that they met the strict criteria of the definition and were truly unavoidable. Government announcements are followed to ensure that signals are reflected in plans.</p> <p>Spending projections built into the Medium Term Financial Plan for 2013/14 are more speculative in the absence of information on funding settlements. The assumptions built into the MTFP have used the best forecast data from the Spending Review and official Treasury forecasts. They have also been subjected to sensitivity analysis.</p> <p>The Reserves strategy has been monitored in the light of Government spending cuts, economic instability and the level of uncertainty and therefore enhanced risk that now pertains. The detailed advice on reserves and balances is included in the budget report.</p>
<p>Savings are not achieved and/or budget growth does not deliver the intended service benefits.</p>	<p>The delivery of savings proposals is being managed through a well-resourced Programme Management Office and overseen by the Corporate Management Team operating as a Transformation Board. Each efficiency them is being led by a Corporate Director with senior responsibility for delivery. Projects and programmes are being managed through robust project management procedures and the delivery of savings is being tracked on an ongoing basis.</p>
<p>Net spending exceeds the approved budget.</p>	<p>There are both service level and corporate budget monitoring procedures in place. Responsibility for monitoring budgets and meeting budget targets is clearly allocated in Financial Regulations to Corporate Directors and Service Heads. The Corporate Management Team receives a monthly report on spending against budgets and ensures that robust action is taken to address issues as soon as they are identified.</p> <p>Regular reports and timetabled and made to the Cabinet. In addition to reserves, provision has been made in budgets for 2011/12 for contingencies against identified budget risks and for the costs of implementing the Medium Term Financial Plan.</p>

	<p>The Programme Management arrangements described above have been dove-tailed into existing monitoring processes to ensure effectiveness and consistency.</p>
<p>The risks of individual budget options are insufficiently explained</p>	<p>All budget options and proposals are set out in pro-forma style, including the risk implications at corporate and service level, and attached as appendices to the budget agenda.</p> <p>Members have received advice from officers about the submission of supplementary proposals at any stage of the budget process that they must all be subject to comments from the relevant senior officer and the Chief Finance Officer.</p>
<p>Core assumptions on pay and price inflation are unrealistic.</p>	<p>Corporate budget preparation guidelines are issued during the summer providing common assumptions about pay and price inflation to ensure consistency between service budgets and between the General Fund and the HRA.</p> <p>The assumptions are reviewed and agreed at a Corporate Financial Services Managers' forum. Levels of inflation and economic forecasts are kept under review throughout the budget process. A sensitivity analysis is carried out to ensure that where projections are inaccurate, the budgetary impact is manageable.</p> <p>Directorate budgets are cash limited.</p>
<p>The budget does not incorporate unavoidable cost pressures and known developments.</p>	<p>The medium term financial planning process is now embedded in the Council's strategic management framework and the budget for 2011/2012 and Medium Term Plan has been substantially derived from the Financial Outlook and Review. The opportunity exists to bring forward cost pressures that were not known about earlier in the process.</p> <p>The Capital Strategy ensures that the revenue impact of capital investment is identified and incorporated in financial plans.</p> <p>There are both service level and corporate budget monitoring procedures. Budget variances in the current year arising from unavoidable cost pressures have fed into the 2011/2012 budget process in the form of committed growth bids.</p>

- 17.3 An assessment of key risk areas relating to individual service budgets has also been undertaken (set out at **Appendix E**) allied to Directorate specific statements of assurance and advice on balances, contingencies and reserves is set out elsewhere in this report. Taking account of those measures, the Corporate Director (Resources) is satisfied that the budget process has been sufficiently robust to assure Members that the proposals included within it can deliver a balanced, sustainable budget.

18. COUNCIL TAX 2011/2012

- 18.1. As part of its decision making this evening, the Council needs to recommend a Council Tax for 2011/12. The Band D Council Tax implied by the decisions

taken ahead of this meeting and the recommendations included in the report is for a Band D Council Tax of £885.52, which is no increase over the Council Tax for 2010/11.

- 18.2. Tower Hamlets' Council Tax is currently 11% below the average Band D Council Tax for London Boroughs in 2010/11, and the sixth lowest Band D Council Tax in London.
- 18.3. The Council collects Council Tax on behalf of itself and the Greater London Authority and pays the resulting income into a Collection Fund for distribution. Any deficit on the Collection Fund at the end of the financial year must be recovered in the following year and the impact is split between the preceptors (the Council and the GLA) in proportion to their Band D Council Tax. Similarly any surplus must be redistributed in the same way. It is estimated that the Collection Fund will have a surplus as at 31st March 2011 and £2.549m will be allocated by the Council in its budget as its share of this surplus.
- 18.4. For 2011/12, the Government has announced that it will provide a Council Tax Freeze Grant to authorities that set a Council Tax increase at 0%. The funding will be equivalent to the difference between a 0% Council Tax and raising 2010/11 Council Tax by 2.5 per cent. The grant applies only to the Council tax set in 2011/12 but will continue to be provided for the four years of the Spending Review. The indicative amount of grant for Tower Hamlets is £1.961m, and for the purposes of this report and for the Medium Term Finance Plan, it is assumed that the authority will set its Council Tax at 0% and receive the grant. The effect of the grant is that if the Council sets any increase in Council Tax between 0% and 2.5%, it will lose more grant income by doing so than it will gain in Council Tax income. Above 2.5%, each 1% increase in Council Tax raises £787,000.
- 18.5. The following table shows examples of the total budget associated with different levels of Council Tax.

<u>Table 18.5 – Council Tax Examples</u>	Budget	Council Tax	Change
	£M	£/Band D	%
2010/2011	310.4	885.52	-
2011/2012			
◆ No Council Tax increase	314.7	885.52	NIL
◆ Council Tax increase of 2.5% - Government's long term inflation target	316.7	907.69	2.5%
◆ Council Tax increase of 4.5%- current rate of inflation (RPI)	318.3	925.37	4.5%

This demonstrates that a fairly significant change in Council Tax has only a relatively small impact on the Council's budget in the context of the savings targets the Council is seeking to deliver.

- 18.6. These examples are for illustration only and they may need to be amended to take account of the final Formula Grant announcement (due in late January/early February) and the surplus on the Collection Fund (see 18.3 above) will need to be reassessed in the final stages of the budget process in accordance with statutory requirements.

Greater London Authority Precept

- 18.7. The GLA precept needs to be added on to Tower Hamlets' Council Tax. The statutory deadline for this announcement is 1st March. The Mayor is currently consulting on a draft budget which would set the GLA's Council Tax for 2011/12 at the same level as for 2010/11. The GLA does not plan to consider and approve its budget until 23rd February. Tower Hamlets Council is not able to reject the GLA's budget; the Local Government Finance Act 1992 requires only that the Council adds the GLA's Council Tax to its own in order to calculate the total tax liability for residents of the borough.

Council Tax Base

- 18.8. The Council Tax Base for the authority for 2011/12 as approved by the Cabinet in January is 88,917.

Budget Capping

- 18.9. Legislation enables the Secretary of State to cap local authority budgets which he deems to be excessive. There are two options open to Ministers; either they can require an authority to recalculate its budget for the year ahead, or they can place an authority on notice that its budget will be capped unless it restrains its budget in the following financial year.

19. BUDGET SETTING TIMETABLE

- 19.1. Following this evening's meeting, a recommended budget requirement and Council Tax will be referred for consideration by the Full Council at its special budget meeting on 23rd February. The setting of Council Tax is a matter reserved to the Full Council by legislation.
- 19.2. The Greater London Authority is also meeting on 23rd February to consider the Mayor's budget proposal for the GLA and the outcome will be reported to Budget Council at the meeting.

- 19.3. The authority is legally required to set a Council Tax before 11th March in any financial year. Notwithstanding this, the Council's local billing arrangements are dependent upon the Council Tax being set in accordance with the Council's established calendar.

20. COMMENTS OF THE CHIEF FINANCIAL OFFICER

The comments of the chief financial officer have been incorporated into this report of which he is the author.

21. CONCURRENT REPORT OF THE ASSISTANT CHIEF EXECUTIVE (LEGAL SERVICES)

- 21.1. The Council is required each year to set an amount of council tax. The obligation arises under section 30 of the Local Government Finance Act 1992 ("the 1992 Act") and must be done by 11 March each year for the following year. In order to set council tax, the Council must calculate the budget requirement in accordance with section 32 of the 1992 Act. This requires consideration of estimated revenue expenditure in carrying out Council functions, estimated payments into the general fund, allowances for contingencies and required financial reserves, amongst other things.
- 21.2. Both the setting of council tax for a financial year and calculation of the budget requirement are matters that may only be discharged by the full council. This is specified in section 67 of the 1992 Act and the Council's Constitution reflects the statutory requirement.
- 21.3. Before calculating the budget requirement, the Council is required by section 65 of the 1992 Act to consult with persons or bodies who the Council considers representative of persons who are required to pay non-domestic rates under the Local Government Finance Act 1988.
- 21.4. The Council's Constitution includes the Budget and Policy Framework Procedure Rules, which specify a process by which the budget is to be developed. The process includes consultation with the Overview and Scrutiny Committee and the report properly recommends that Cabinet consider the views of the Overview and Scrutiny Committee before determining its proposals for submission to full Council.
- 21.5. In circumstances where the Council is calculating the budget requirement, the chief finance officer (the Director of Resources) is required by section 25 of the Local Government Act 2003 to report on the following matters: the robustness of the estimates made for the purposes of the calculations; and the adequacy of the proposed financial reserves. The Council is required to have regard to the chief finance officer's report before calculating the budget requirement.

- 21.6. The report appropriately brings forward relevant financial information concerning the setting of council tax and calculation of the budget requirement. It sets out the results of consultation with payers of non-domestic rates and other consultation. It sets out the chief finance officer's views the robustness of estimates and the adequacy of reserves. It is open to Cabinet to agree the base budget, growth and savings figures that form part of the calculation and to recommend to the full council the budget requirement and council tax as proposed.
- 21.7. The report otherwise recommends that Cabinet agree the medium term financial plan. This is a matter that informs the budget process and may be viewed as a related function. It is, in any event, consistent with sound financial management and is a matter that is open to the Cabinet.

22. ONE TOWER HAMLETS CONSIDERATIONS

- 22.1 The setting of the Council's budget is a complex and lengthy process which involves consultation with the general public, businesses and Members of the Council through the Budget and Policy Framework. The budget is set in the context of the Community Plan, which takes account of the needs of all sections of the community living, working in Tower Hamlets and visitors.
- 22.2. High quality information on the equality impact of savings proposals is necessary to enable budget decisions to be taken in an informed, fair and transparent way. At a time of significant financial pressure, this is essential to maintaining the Council's policy of tackling inequality and disadvantage, as well as fulfilling the authority's legal duties.
- 22.3. The table below outlines the process, which has been developed in consultation with the Council's Corporate Equalities Steering Group, that is being employed to equality impact assess all budget proposals.

Who	Output	When
Service Managers/ Directors	Screening of individual savings proposals	December
Dedicated team	Aggregated Equality Impact Assessments of major savings themes	January 2011
	Budget Equality Impact Assessment	January 2011
Tower Hamlets	Community Plan Equality Impact Assessment	February 2011

Partnership	Fairness Commission to track local impact and revisit approach	2011/ 2012
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- 22.4. Every savings proposal has been individually screened against a checklist of critical questions to assess the potential equality impact for communities and staff. A summary of the equality implications and completed screening assessment is included within each budget proposal attached at **Appendix D**. Full impact assessments for proposals that are identified to have significant equality implications including their cumulative impact will be made available on the Council website before the end of the first week in February.
- 22.5. As part of the Community Plan refresh, officers will also work with the Tower Hamlets Partnership to understand the cumulative equality impact of savings that are to be made borough wide across partner organisations. This will inform the development of focused equality priorities for the refreshed Community Plan, which will aim to ensure that limited resources are targeted at the most significant inequality gaps at risk of further widening in the next period.
- 22.6 Although these equality impact assessments will help anticipate the likely effects of proposals on different communities and groups, in reality the full impact of a decision will only be known once it is introduced. The actual impact of the implemented savings proposals will therefore be reviewed through a Fairness Commission in 2011/12.

23. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

The SAGE implications of individual proposals in the budget are set out in the papers relating to those proposals.

24. RISK MANAGEMENT IMPLICATIONS

Managing financial risk is of critical importance to the Council and maintaining financial health is essential for sustaining and improving service performance. Setting a balanced and realistic budget is a key element in this process. Specific budget risks are set out in Section 15 of this report.

25. CRIME AND DISORDER REDUCTION IMPLICATIONS

The CDR implications of individual proposals in the budget are set out in the papers relating to those proposals.

26. **EFFICIENCY STATEMENT**

The Council is required to consider the value for money implications of its decisions and to secure best value in the provision of all its services. It is important that, in considering the budget, Members satisfy themselves that resources are allocated in accordance with priorities and that full value is achieved. The information provided by officers on committed growth and budget options assists Members in these judgments.

27. **APPENDICES**

Appendix	Title
Appendix A	Base Budget and Base Directorate Targets 2011/12
Appendix B	Potential Committed Growth 2011/12 – 2013/14
Appendix C	Medium Term Financial Plan 2011/12- 2013/14
Appendix D	Savings Summary and Detail
Appendix E	Strategic & Corporate Risks
Appendix F	Reserves and Contingencies
Appendix G	General Reserves as at 31 st March 2011
Appendix H	Budget Consultation for 2011/12 (to follow)

Local Government Act, 1972 Section 100D (As amended)
List of “Background Papers” used in the preparation of this report

Brief description of “background papers”	Name and telephone number of holder and address where open to inspection.
None	F

