| Cabinet<br><br>11 July 2022 | TOWER HAMLETS |
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| **Report of:**<br>Kevin Bartle, Interim Corporate Director - Resources (Section 151 Officer) | **Classification:**<br>Unrestricted |
| **MTFS and Budget Scene Setting 2023-26** | |

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| **Lead Member** | **Councillor Saied Ahmed, Cabinet Member for Resources and the Cost of Living** |
| **Originating Officer(s)** | Kevin Bartle, Interim Corporate Director - Resources |
| **Wards affected** | All wards |
| **Key Decision?** | No |
| **Forward Plan Notice Published** | May 2022 |
| **Reason for Key Decision** | N/A |
| **Strategic Plan Priority / Outcome** | 1. People are aspirational, independent and have equal access to opportunities;<br><br>2. A borough that our residents are proud of and love to live in;<br><br>3. A dynamic outcomes-based Council using digital innovation and partnership working to respond to the changing needs of our borough. |

## Executive Summary

The Council's Budget 2022-23 was approved by Full Council in March 2022. This report summarises the review of the MTFS as part of the 2023-24 budget setting process.

Despite the Chancellor announcing departmental spending limits for Government departments on 27 October 2021 for three years, 2022-23 to 2024-25, the Local Government Finance Settlement (LGFS) was only announced for a single year covering 2022-23. The funding landscape for Local Government over the medium term remains highly uncertain. Core Grants such as the Revenue Support Grant, New Homes Bonus and the Improved Better Care Fund were rolled forward for 2022-23, with additional funding received via the Social Care Grant, with much of this expected to contribute to additional costs arising from Adult Social Care Reforms. There was also a one-year one-off Services Grant distributed to Local Authorities for 2022-23.

One reason Councils were provided with a single year settlement was due to funding

reforms that have been delayed, annually, for several years that the Government has signalled its intention to now take forward. The distribution formula utilised for allocating resources across Local Authorities dates to 2013-14 and the Government propose to take forward a ‘Fair Funding Review’ to ensure a more up to date assessment of need. Business Rate Baselines have not been reset since 2013-14 and, therefore, Councils that have experienced growth in their Business Rates have been able to retain a share of growth since that year. The Government intends to reset the Baselines to coincide with a review of the funding formula. In early 2021 the Government consulted on ending New Homes Bonus (NHB), a targeted incentive providing funding based on housing growth within the Council area, and the Government has not yet announced the outcome of its consultation.

The impact of these funding reforms is particularly acute for Tower Hamlets. Funding retained from Business Rates Growth and the New Homes Bonus are significant and therefore the impact of resetting the Business Rates baseline or withdrawing New Homes Bonus would result in a substantial funding reduction for the Council. The Government has indicated that transitional relief would be provided to Councils who were impacted by the reforms. At this stage it is not clear when the reforms will be introduced nor what transitional relief would look like.

For 2022-23 the Council benefitted from rolled forward funding and new grants provided. The Council was therefore able to set a balanced budget and to propose a freeze in the Tower Hamlets element of Council Tax, only levying the 1% Adult Social Care precept to meet demographic pressures within that area. It will therefore be important to continue work to balance the budget over the medium term, ensuring alignment with the refreshed strategic plan.

The impact of inflation has significantly increased in recent months with high fuel and energy costs and food prices. As of April 2022, RPI Inflation was at 11.1% and CPI inflation at 9% and high inflation has a direct impact on the council’s contracts and fuel and energy costs. The societal impacts of rising prices will also mean more individuals will require council support going forward. The latest treasury forecasts show high inflation through 2022-23 but reducing back to a lower level over the medium term.

The Coronavirus pandemic continues to have a residual impact on the Council’s cost of services and reductions in income, forecast to be met in the short term by one-off Covid grant. The ongoing scale of the impact on society, the economy and public finances resulting from Covid-19, Brexit and recent inflationary pressures in the medium to long term is at this point unknown.

As previously, consultation with residents, businesses and other key stakeholders will be a feature of proposed changes and the results of the Council’s 2023-24 budget consultation will be considered at Cabinet in October.

The MTFS will be updated throughout 2022 as the Chancellor’s Autumn Statement and the provisional Local Government Finance Settlement (LGFS) are announced.

This report examines the key issues and pressures facing the Council in the medium term, with an updated position on funding, growth pressures and saving requirements. Continued focus on identifying and delivering efficiencies for future years will play a central role in ensuring financial sustainability going forward.

**Recommendations:**

The Mayor in Cabinet is recommended to:

1. Note the current General Fund Revenue Funding Requirement of **£421.500m** for 2023-24 prior to the budget setting review to be carried out in year.

2. Note the budget gap assuming a 0% council tax increase compared to the normally permitted 1.99% and the implications on Adult Social Care funding if the Council was not able to levy the assumed 1% Adult Social Care Precept.

3. Note the latest draft position of the Council's reserves, subject to sign off of the statements of accounts.

4. Note that currently £1m funding from the Public Health grant is allocated to the Key Stage Two extension of Free School Meals as well as £2m from the Free School Meals Reserve.

5. Note that any increase in the Social Care Grant for 2023-24 is assumed to be allocated in full to the services (75% to adult social care and 25% to children's social care).

6. Note that the HRA housing rent and service charge increases will require consideration once the September 2022 CPI inflationary figure is known.

7. Note that the 2022-23 Management Fee payable to Tower Hamlets Homes (THH) was increased from £33.236m to £33.676m following addition of the 2021-22 pay award.

8. Note that under the Management Agreement between the Council and THH, THH manages delegated HRA income and expenditure budgets on behalf of the Council. In 2022-23, THH is managing delegated income budgets totalling £98.842m and delegated expenditure budgets totalling £32.128m.

9. Note the current assumption that the Local Council Tax Reduction Scheme will remain unchanged for 2023-24.

10. Note the Equalities Implications as set out in Section 4.

## 1. REASONS FOR THE DECISIONS

1.1 The Council is under an obligation to set a balanced and sustainable budget and to set the Council Tax Levels for the financial year 2023-24 by 11 March 2023 at the latest. The Council's Chief Financial (S151) Officer must confirm the robustness of the estimates applied and the adequacy of the Council's reserves as part of the budget setting report to Council.

1.2 The setting of the budget is a decision reserved for Full Council. The Council's Budget and Policy Framework requires that a draft budget is issued for consultation with the Overview & Scrutiny Committee to allow for their comments to be considered before the final budget proposals are made to Full Council.

1.3 The announcements and consultations made about Government funding for the Council in the Chancellor's Spending Review, the Local Government Finance Settlement, challenges such as high inflation and the impact of the Covid-19 pandemic require a robust and timely response to enable a balanced budget to be set.

1.4 A Medium Term Financial Strategy (MTFS) covering the entirety of the resources available to the Council is considered to be the best way that resource prioritisation and allocation decisions can be considered and agreed in a way that provides a stable and considered approach to service delivery and takes into account relevant risks and uncertainty.

1.5 As the Council develops its detailed proposals it must continue to keep under review those key financial assumptions which underpin the Council's MTFS. Significant funding reforms have been signalled by Government and the Council has a reliance on funding sources that are potentially subject to change significantly in the Medium Term, and therefore it is important to continue to monitor the Medium Term position.

1.6 The Mayor is required by the Local Government and Housing Act 1989 to determine a balanced Housing Revenue Account (HRA) budget prior to the start of the new financial year. The Council must also approve the Management Fee payable to Tower Hamlets Homes (THH) so that it can fulfil its obligations under the Management Agreement to manage the housing stock on behalf of the Council.

1.7 In accordance with Financial Regulations, capital schemes must be included within the Council's capital programme, and capital estimates adopted prior to any expenditure being incurred. Capital will be subject to a separate report to Cabinet in July and the setting of capital budgets for the medium term will be aligned to revenue budget setting during the year.

## 2. <u>ALTERNATIVE OPTIONS</u>

2.1 Whilst the Council will adopt a number of approaches to the identification of measures aimed at delivering its MTFS it must set a legal and balanced budget and maintain adequate reserves. The scale of the changes experienced mitigate against continuing on the basis agreed in March 2021 without a re-appraisal of both the financial and policy position.

2.2 The Council is required 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 Council can determine its priorities in terms of the services it seeks to preserve and protect where possible, and to the extent permitted by its resources, those services it wishes to prioritise through investment.

2.3 The Council has a statutory duty to set a balanced HRA and provide THH with the resources to fulfil its obligations under the Management Agreement. Whilst there may be other ways of delivering a balanced HRA, the budget setting process outlined in this report is considered the most effective, in realising all the Council's statutory duties having regard to the matters set out in the report.

## 3. DETAILS OF THE REPORT

### 3.1 BACKGROUND

3.1.1 The medium-term financial planning process is an essential part of the Council's resource allocation and strategic service planning framework. The MTFS integrates strategic and financial planning over a multi-year period. It translates the Strategic Plan priorities into a financial framework that enables the Mayor and officers to ensure policy initiatives can be delivered within available resources and can be aligned to priority outcomes.

3.1.2 The drivers for the Council's financial strategy are:

- To set a balanced budget over the life of the MTFS whilst protecting residents from excessive Council Tax increases, as defined by the government, through the legislative framework covering Council Tax referenda.
- To fund priorities agreed within the Strategic Plan, ensuring that service and financial planning delivers these priorities.
- To deliver a programme of planned reviews and savings initiatives designed to keep reductions to service outcomes for residents to a minimum.
- To maintain and strengthen the Council's financial position so that it has sufficient contingency sums, reserves and balances to address any future risks and unforeseen events without jeopardising key services and delivery of service outcomes for residents.
- Ensuring the Council maximises the impact of its spend to deliver priority outcomes in the context of reducing resources.

### 3.2 STRATEGIC APPROACH

3.2.1 Budget setting during the year will be aligned with strategic planning for the authority, outlining the priorities for the new administration and aligning resources with key priority areas.

## 3.3 PROPOSED BUDGET

3.3.1 The refreshed MTFS is set out in Appendix 2A, and the detail by service area in Appendix 2B. The detailed figures and assumptions incorporated in these tables are explained more fully in this report.

3.3.2 The previous multi-year funding settlement agreed with the Government expired at the end of the 2019-20 financial year. Single year settlements were announced for first 2020-21, then 2021-22 and now 2022-23. The government announced the Spending Review 2021 on 27 October 2021, which provided resource budgets for Government Departments the three years 2022-23 to 2024-25. However, the Government only announced **a single year** provisional Local Government Finance Settlement (LGFS) for 2022-23, published on 16th December 2021, to enable funding reforms to be progressed. The absence of a long-term settlement hinders the ability of Local Authorities to plan for the Medium Term effectively.

3.3.3 Previously the direction of travel for Local Authority funding reflected a move away from direct general government support such as through Revenue Support Grant towards more targeted grant support coupled with an increased reliance on locally generated sources of income such as Council Tax, retained Business Rate growth and targeted incentive payments such as New Homes Bonus funding. Following the pandemic, the Government has signalled a change in direction consulting on ending New Homes Bonus payments and progressing a ‘fair funding review’ to assess needs and a business rates reset. The needs assessment formula utilised to distribute funding and business rates baselines have been unchanged since 2013-14 and a review of these will have significant implications for Tower Hamlets over the medium term. It is anticipated these reforms will be implemented on 1 April 2023 at the earliest and transitional relief will be provided to councils who will lose funding as a result. Given the lack of any announcement thus far, it is not expected that reforms will come into place until 1 April 2024.

3.3.4 The impact of the Covid-19 pandemic has inevitably impacted on the level of resources available and shaped the government’s own short-term funding priorities. This means both the relative priority of local government against other government departments such as the NHS as well as the relative resource allocations between local government services. Since March 2020 the Government has announced various packages of one-off funding to Councils to support Local Authorities through the pandemic, including enabling Councils to defer the costs of deficits in Council Tax or Business Rates collection over multiple years. The long-term pressures on the Council’s finances of the pandemic remain to be quantified.

## 3.4 IMPACT ON COUNCIL SERVICES

3.4.1 The one-year provisional Local Government Finance Settlement (LGFS) for 2022-23 was positive for Tower Hamlets as funding streams that were expected to come to an end were rolled forward for an additional year. This includes New Homes Bonus funding and another year of business rates growth, that Tower Hamlets has been able to retain since the baselines were set in 2013-14. There was also additional Social Care Grant and a one-off Services Grant for 2022-23. This enabled the Council to set a balanced budget for 2022-23 whilst freezing its element of Council Tax, aside from levying a 1% precept specifically for Adult Social Care to fund demographic pressures in that area.

3.4.2 The Government has signaled that the one-year settlement was provided to facilitate taking forward Local Government funding reforms including a 'fair funding' review of the needs assessment formula and a reset of Business Rates baselines essentially wiping-out growth since 2013-14. In early 2021 the Government also consulted on altering New Homes Bonus funding, with the outcome expected to be published in 2022.

3.4.3 The proposed changes would have significant implications for Tower Hamlets over the Medium Term. Retained Business Rates above the Council's baseline accounts for approximately £18.8m of the Council's funding and New Homes Bonus funding is expected to be £12.9m in 2023-24. If these funding sources are removed it is not clear how the money would be redistributed across Local Government, although the Government has signaled transitional relief would be provided to Councils to support them managing funding reductions. It is uncertain when any such reforms would come into place.

3.4.4 In addition to funding uncertainties in the medium term, the Council continues to face increases in demand for services, inflationary cost increases and demographic cost pressures particularly in Adult Social Care. The long-term impacts of the ongoing coronavirus pandemic remain uncertain.

3.4.5 The majority of the Council's costs relate to staffing and, given the scale of the challenges projected for future years, it is likely that continuing significant reductions will be needed to the Council's overall headcount and pay bill. The processes by which posts are identified draw upon the lessons learnt during the pandemic about which services are essential, which services are discretionary and which service delivery points are required for the future delivery of what are likely to be changed or redesigned services.

## 3.5 FINANCIAL RESOURCES

Table showing MTFS based on assumed general Council Tax increase of 0% for all years:

| MTFS Summary 2023-26 | 2023-24 £'000 | 2024-25 £'000 | 2025-26 £'000 |
|---|---|---|---|
| **Net Service Costs** | 389,473 | 421,500 | 438,256 |
| Growth - Previously approved by Full Council | 137 | - | - |
| Growth - New | 12,342 | 9,157 | 6,266 |
| Inflation - Previously approved by Full Council | 6,500 | - | - |
| Inflation - New | 17,300 | 10,000 | 6,900 |
| Savings - Previously approved by Full Council | (7,181) | - | - |
| Savings - Write back of previously approved Savings | - | - | - |
| Savings - New (reprofiling & write-offs or approved savings) | 2,929 | (2,400) | (100) |
| **Total Funding Requirement** | **421,500** | **438,256** | **451,322** |
| | | | |
| Core Grants: | | | |
| - Revenue Support Grant | (36,883) | (37,617) | (38,369) |
| - New Homes Bonus | (2,328) | (2,328) | (2,328) |
| - New Homes Bonus - transitional funding (via Services Grant) | (10,550) | (10,550) | (10,550) |
| - Improved Better Care Fund | (16,810) | (16,810) | (16,810) |
| - Social Care Grant | (16,602) | (16,602) | (16,602) |
| - Public Health Grant | (39,315) | (40,101) | (40,903) |
| - Rough Sleeping Initiative | (658) | (672) | (672) |
| - Homelessness Prevention Grant | (6,062) | (6,183) | (6,183) |
| - Market Sustainability and Fair Cost of Care Fund | (8,546) | (12,208) | (12,208) |
| - Lower Tier Services Grant | (1,479) | (1,479) | (1,479) |
| **Core Grants** | **(139,232)** | **(144,550)** | **(146,104)** |
| **Business Rates** | **(150,596)** | **(147,970)** | **(155,122)** |
| Council Tax: | | | |
| - Council Tax - in year income | (128,226) | (134,702) | (140,863) |
| - Council Tax - Collection Fund deficit / (surplus) | 364 | - | - |
| **Council Tax** | **(127,862)** | **(134,702)** | **(140,863)** |
| **Total Funding** | **(417,690)** | **(427,221)** | **(442,090)** |
| | | | |
| **Budget Gap / (Surplus)** | **3,810** | **11,035** | **9,233** |
| **Contribution to Reserves / (Drawdown from Reserves)** | **(3,810)** | **(11,035)** | **(9,233)** |
| **Budget Gap** after Contribution / (Drawdown) to Reserves | **0** | **0** | **0** |

Assumptions:

- No increase in General Council Tax for all years.
- ASC precept increase of 1% for all years - allocated to fund ASC demography.
- Business Rates income - assumes reset to occur in 2025-26 but partially offset by transitional funding (75% in 2025-26).
- New Homes Bonus - assumes transitional funding to retain funding level at current income (excluding legacy payments).
- Market Sustainability and Fair Cost of Care Fund grant fully given to services (primarily Adult Social Care for reduced client contribution income).
- Pay Inflation - 4% for 2022-23 and 2023-24; 2% for other years.
- Contractual Inflation - 4.5% for 2022-23; 6% for 2023-24; 4% for 2024-25; 2% for 2025-26.

Please note: If the ASC Precept was not able to be applied, this would not increase the budget gap per se, but would decrease the resources given to ASC (c£1.3m in 2023-24, c£2.7m in 2024-25 and c£4.2m in 2025-26).

**Council Tax**

3.5.1 Council Tax income is a key source of funding for Council Services. The amount generated through Council Tax is principally determined by the Council Tax Base (the number of properties adjusted for exemptions and discounts) and the rate of charge per property.

3.5.2 The Council currently can, subject to legislative constraints, increase its Council Tax rate through two mechanisms; the Adult Social Care precept and general tax rate increases.

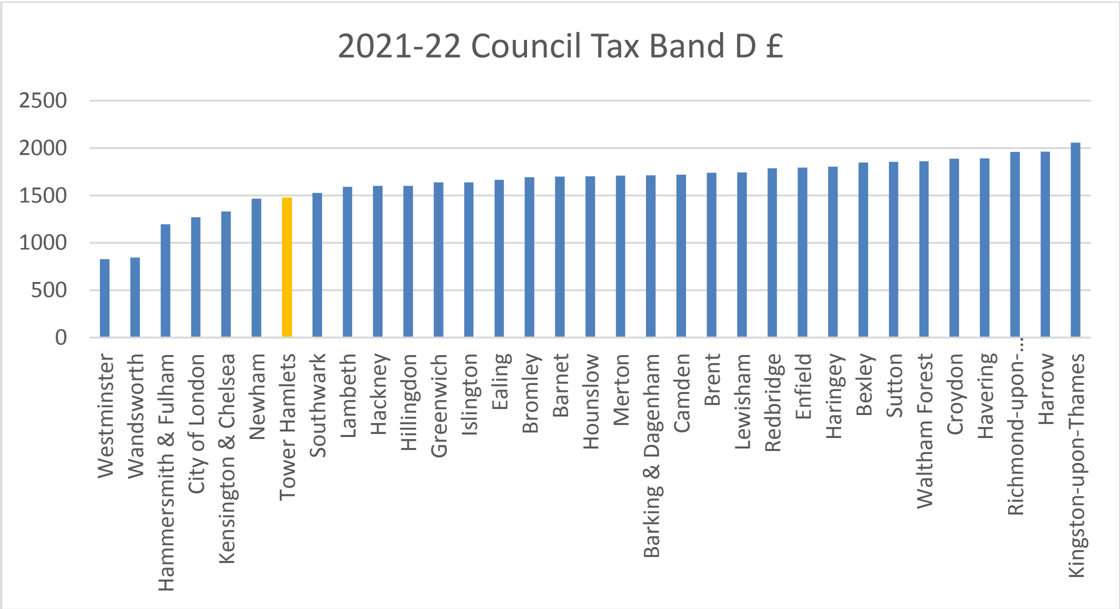
3.5.3 If the Council was to implement a general increase to Council Tax, **each 1%** would generate extra income (and therefore decrease the budget gap) of c£1.3m in 2023-24, c£2.7m in 2024-25 and c£4.2m in 2025-26).

3.5.4 For the Adult Social Care (ASC) precept, specifically to fund Adult Social Care pressures, the government agreed a maximum level of 1% for 2022-23 and the Council consulted on and implemented a 1% precept. The Council did not implement an increase in the general Council Tax rate for 2022-23.

3.5.5 The government has not stated to date what the referendum level for general tax rate increases will be (in recent years this has been 1.99%) and whether an ASC precept will be allowed for 2023-24. The government assumes in the Core Spending Power calculation that Councils will increase Council Tax at the maximum allowed level. If the Council, therefore, does not implement at the maximum level, then its spending power to provide services would be reduced going forward with no funding from government to mitigate this.

3.5.6 Currently Tower Hamlets has one of the lowest Council Tax rates across the 33 London Boroughs as shown in Chart 1 below.

**Chart 1: 2021-22 Council Tax Rates Across London**




3.5.7 The borough has seen increases in the number of new homes over the last few years, however the Covid-19 pandemic has had a material impact on the level of income received from this source; the virus has impacted the number of people in work or receiving low pay and as a consequence increased significantly those claiming benefits, including through the Local Council Tax Reduction Scheme (LCTRS). There has also been a drop in the collection rate as residents have been affected by Covid-19 on their income levels.

3.5.8 The Mayor in Cabinet approved the Council Tax Base calculation for 2022-23 on 18 January. The Council Tax Base calculation assumed growth of 3.5% in 2022-23 and a 97.50% collection rate and the estimate of the 2023-24 Tax Base will be calculated later in 2022.

**Local Council Tax Reduction Scheme (LCTRS) 2022-23**

3.5.9 In March 2022, the Council agreed that there would be no changes to the current Local Council Tax Reduction Scheme (LCTRS) for 2022-23. Due to the impacts of the pandemic, the cost of the scheme rose from £26.7m in 2019-20 to £31.6m in 2020-21. The level of claimants has reduced slightly from the increased pandemic level (£32.7m cost in 2021-22 which includes the effect of the annual Council Tax increases), however the impact of the current higher cost of living may impact the levels of claimants in the future.

3.5.10 The current LCTRS scheme remains amongst the most generous in the UK protecting Tower Hamlets residents on low incomes. Those on the lowest income are able to receive 100% relief and pay no Council Tax.

3.5.11 Each year, the Council is required to consider whether it wishes to change its LCTRS. Any changes to the scheme require a full public consultation and impact analysis.

3.5.12 The budget assumes that the existing 100% LCTRS will remain unchanged for 2023-24 protecting our residents on low incomes.

**Settlement Funding Assessment and Revenue Support Grant**

3.5.13 Settlement Funding Assessment (SFA) reflects the government's current approach to funding most local authorities through Revenue Support Grant (RSG) and retained business rates.

3.5.14 Each authority's SFA is based on a needs assessment established at the beginning of the funding arrangements and thereafter reflecting the impact primarily of government funding reductions. The Baseline Funding Level represents the amount of retained business rates that the government expects each local authority to generate assuming no increase in the tax base since the scheme inception (i.e. it continues to increase only in line with the increase in the relevant business rate multiplier).

3.5.15 The difference between SFA and the Baseline Funding Level is the amount of RSG an authority receives. For Tower Hamlets, the 2022-23 calculation based on the Provisional Local Government Finance Settlement is shown below.

**Settlement Funding Assessment**

| Settlement Funding Assessment | 2021-22 £m | 2022-23 £m |
|---|---|---|
| Settlement Funding Assessment (SFA) | 145.5 | 146.6 |
| Baseline Funding Level (BFL) | 111.5 | 111.5 |
| Revenue Support Grant (RSG) | 34.0 | 35.1 |

**Business Rates Retention Scheme**

3.5.16 The Council has entered a business rates pool with seven other neighbouring London Boroughs in 2022-23 (the 8 Authority Pool) which will enable the Council to retain some of the levy on growth that would otherwise be required to be paid to Central Government. The amount of extra growth retained was estimated to be £2.5m one-off extra income in 2022-23.

3.5.17 The Covid-19 pandemic significantly impacted the business rates income for the Council and created a 2020-21 Business Rates Collection Fund deficit which will be required to be repaid over the period 2021-24. The Council share of the accumulated Business Rates deficit to the end of 2020-21 is £55.0m (primarily funded through government grants for business rates reliefs), towards which the government will also provide compensation of £14.1m. The deficit reduced due to the removal of the provision for Material Change in Circumstances (MCC) appeals, following government legislation, which excluded the ability for businesses to request revaluations based on the short term effect of the Covid pandemic.

3.5.18 The Council is utilising its Collection Fund Smoothing Reserve to align the government grant funding of business rates reliefs with the timing of deficit payments over the three-year period 2021-24. The Covid-19 pandemic continued to have a significant impact on the 2021-22 business rates income through revaluations, other changes to the rating list and a reduction in collection rates.

3.5.19 The business rates baseline was due to be reset in 2022-23, however this has been delayed until at least 2023-24. The refreshed MTFS currently assumes that this will be delayed further until 2025-26 (due to the lack of any announcement and due to recent indications by Local Government Finance in DLUHC) and partially offset by transitional funding (75% in 2025-26).

3.5.20 The current business rates system allows councils to retain a proportion of the growth in the local business rates tax base, however this is typically lost during funding rebasing. For Tower Hamlets this is c£18.8m of funding that could be lost because of a reset and the annual delays have improved the budget position in recent year and it is forecast this will continue for 2023-24 and 2024-25. The Government has signalled funding reforms to be implemented as part of the Levelling Up agenda which could encompass the reset of business rates baselines and allocations across the country. There is significant uncertainty around when the government will implement the reset, how the money would be redistributed across Local Government and the amount of any transitional relief provided to the Council; therefore, the level of business rates income is uncertain over the medium term with a risk of reduced funding for the Council going forward.

**Collection Fund**

3.5.21 Due to the effect of the Covid-19 pandemic on the Collection Fund deficits for 2020-21, the government announced that 2020-21 deficits can be repaid over the three-year period 2021-24. This is a further spread of the impact over more years than the normal requirements for repayment periods. Furthermore, the Spending Review 2020 announced that the government will fund 75% of components of the 2020-21 deficit.

3.5.22 There is an accumulated Business Rates Collection Fund deficit to the end of 2020-21, of which the Council share is £55.0m (primarily funded through government grants for expanded retail and nursery scheme business rates reliefs). The Council is utilising its Collection Fund Smoothing Reserve to align the government grant funding of business rates reliefs with the timing of deficit payments over the three-year period 2021-24. The Collection Fund currently remains under consideration by external audit and, therefore, the accumulated deficit to the end of 2020-21 may be subject to change.

3.5.23 The Business Rates accumulated deficit includes a significant increase in the loss allowance (bad debt provision) for potential non-payment of debts to the Council, again due to the pandemic, rising £5.8m (Council share) from £1.9m (2019-20) to £7.7m (2020-21).

3.5.24 There is an accumulated Council Tax Collection Fund deficit to the end of 2020-21, of which the Council share is £6.5m. The government has compensated £2.0m of this (being 75% of certain components of the 2020-21 gross deficit). The deficit includes the impact of the loss allowance (bad debt provision) which was increased by £2.9m (Council share) from £11.9m (2019-20) to £14.8m (2020-21) due to the impact of the pandemic.

3.5.25 The Collection Fund Smoothing Reserve has a draft balance of £66.8m at the end of 2020-21, subject to the closure and audit of the Council's accounts for the period 2016 - 2021. This includes Section 31 grant income from central government to fund the expanded retail and nursery scheme business rates reliefs for 2020-21, which will be drawn down over the period 2021-24 to match the years in which the related business rates deficit payments will impact the financial accounts. The purpose of the Smoothing Reserve is also to balance out potential deficits and surpluses across individual years for Business Rates and Council Tax income over the medium term. Income collection to date and forecasts for the year are monitored monthly including the impact of inflation and the pandemic on the Collection Fund.

**Core Grants**

3.5.26 The Council is in receipt of several core grants to support specific service priorities. Given the uncertainty of the Fair Funding review and reforms signalled by the Government but not yet implemented, assumptions have been made in respect of most grants after the announced 2022-23 level. There are risks associated with this approach as the government may decide to change its priorities and reduce or cease funding through a grant or reallocate service specific grants into more general funding with a changed distribution methodology.

**Revenue Support Grant**

3.5.27 Revenue Support Grant (RSG) is a central government grant given to local authorities which can be used to finance revenue expenditure on any service. The amount of Revenue Support Grant to be provided to authorities is established through the Local Government Finance Settlement using the relevant funding formulae; the revision of these formulae is the focus of the (deferred) Fair Funding review process.

3.5.28 The Council's Revenue Support Grant (RSG) has decreased from circa £54m in 2017-18 to £35m in 2022-23.

**New Homes Bonus**

3.5.29 The New Homes Bonus (NHB) scheme was introduced in 2011-12 to help tackle the national housing shortage. The scheme was designed to reward those authorities that increased their housing stock either through new build or by bringing empty properties back into use. Tower Hamlets is a high growth area and has attracted one of the highest levels of NHB in the country.

3.5.30 A consultation was launched after the 2021-22 settlement on the future of NHB with options including increasing the threshold for payment and various other factors that could be included for calculations. There is uncertainty in the amounts to be received going forward and it is likely that payments in future will be significantly lower. The Secretary of State for DLUHC had stated that the government's response to the consultation will be published in early 2022 and that they are committed to reform and will use the additional year to carefully consider how they can ensure the incentive is more focused and targeted on ambitious housing delivery and which complements wider government priorities. An announcement is now expected in the summer which will include potential NHB changes as part of the wider Levelling Up agenda.

3.5.31 If the NHB (including all legacy payments) were to come to an end in the medium term, it is expected that decreases in NHB will be re-allocated nationally into other funding streams such as the Revenue Support Grant or other core grants, however this will clearly need to be kept under review. As part of the provisional LGFS, the Secretary of State for DLUHC announced a further round of New Homes Bonus allocations under the current scheme for 2022-23. The allocations for 2022-23 include previously announced legacy payments but, as in 2021-22, these new allocations for 2022-23 will not result in new legacy commitments being made in subsequent years on those allocations. The New Homes Bonus grant has reduced nationally from £622m in 2021-22 to £554m in 2022-23. The Council's New Homes Bonus grant allocation has decreased from £17.646m in 2021-22 to £16.263m in 2022-23.

3.5.32 Over the medium term the level of funding potentially lost will depend on which changes are announced, the timescales for implementation and any transitional funding for Councils such as Tower Hamlets that would lose significant funds as a result. The amount of funding going forward remains therefore unclear. The MTFS currently assumes that funding would be retained at a similar amount to the 2022-23 allocation but will need to be updated when more information is available.

Table showing NHB allocations for Tower Hamlets 2020-21 to 2022-23:

| **New Homes Bonus** | **2020-21 £m** | **2021-22 £m** | **2022-23 £m** |
|---|---|---|---|
| 2017/18 allocation | 5.406 | | |
| 2018/19 allocation | 6.180 | 6.180 | |
| 2019/20 allocation | 3.812 | 3.812 | 3.812 |
| 2020/21 allocation | 6.584 | | |
| 2021/22 allocation | | 7.654 | |
| 2022/23 allocation | | | 12.451 |
| **Total Allocation** | **21.981** | **17.646** | **16.263** |

### Improved Better Care Fund

3.5.33 The Better Care Fund (BCF) was introduced in the 2013-14 spending review. The fund is a pooled budget, bringing together local authority and NHS funding to create a national pot designed to integrate care and health services.

3.5.34 In addition to this, an Improved Better Care Fund (IBCF) was announced in the 2016-17 budget to support local authorities to deal with the growing health and social care pressures during the period 2017-20. The Spending Rounds since 2019 have extended this grant for one year at a time and the continued provision of this funding is built into the budget.

### Social Care Grant

3.5.35 In the Chancellor's 2019-20 budget, £410m of additional funding was announced for use for adult and children's social services. The government believes there is not a single bespoke needs formula that can be used to model relative needs for both adult and children's social care, therefore the existing Adult Social Care Relative Needs Formula was used to distribute this Social Care Support Grant funding.

3.5.36 The 2020-21 LGFS confirmed that the previous Social Care Support Grant allocations will be rolled into a new Social Care Grant for 2020-21. The Social Care Support Grant allocation for Tower Hamlets of £2.499m was used to support the revenue budget funding for demographic and inflationary growth for the directorates. The grant was increased in 2020-21 to £9.367m. This increase of £6.868m was allocated 50% to supporting the revenue budget funding for demographic and inflationary growth for the directorates, and the remaining 50% directly allocated as budget to the services (75% to adult social care and 25% to children's social care).

3.5.37 The Spending Review 2020 announced a further one-off increase to the Social Care Grant for 2021-22 of £2.974m and this was allocated in full as budget to the services. The 2022-23 LGFS retained the 2021-22 increase and further increased the grant by another £4.261m (to a total £16.602m) and this was also allocated directly to the specified services.

3.5.38 The table below demonstrates the allocations of the Social Care Grant.

| Social Care Grant Allocations | Adult Social Care Budget | Children's Social Care Budget | Funding of Demography and Inflation | Total |
|---|---|---|---|---|
| | £m | £m | £m | £m |
| 2019-20 Funding | - | - | 2.499 | 2.499 |
| 2020-21 Additional Funding | 2.575 | 0.858 | 3.435 | 6.868 |
| 2021-22 Additional Funding | 2.230 | 0.744 | - | 2.974 |
| 2022-23 Additional Funding | 3.196 | 1.065 | - | 4.261 |
| **Total 2022-23** | **8.001** | **2.667** | **5.934** | **16.602** |

### Social Care Reform

3.5.39 In December 2021 the Government published its long-awaited white paper on Adult Social Care reform entitled ‘People at the Heart of Care’ setting out a 10-year vision for transforming support and care in England. The document set out a range of priorities that the Government will seek to take forward with the sector in coming years.

3.5.40 The Government published ‘Build Back Better: Our Plan for Health and Social Care’ in September 2021 introducing a new health and social care levy to National Insurance Contributions, initially to help fund the clearance of NHS backlogs, a cap on care costs of £86,000 and the ability of self-funders to ask their Local Authority to arrange their care for them. The Government announced that the cost of the increased National Insurance Employer Contributions for Councils will be funded and the provisional LGFS stated that the 2022-23 funding has been included in the new Services Grant, although the grant is one-off whilst the tax increase is permanent.

3.5.41 The LGFS has stated that to ensure that local authorities are able to move towards paying a fair cost of care, the Government is providing an additional £1.4 billion over the next 3 years. This forms part of the £3.6 billion confirmed at Spending Review 2021 to implement Charging Reform. £162 million will be allocated in 2022 to 2023 to support local authorities as they prepare their markets for reform. A further £600 million will be made available in both 2023-24 and 2024-25. These proposals are funded by the new Health and Care Levy announced in September 2021, of which £5.4 billion is being invested into adult social care over the next 3 years. Beyond the next 3 years, an increasing share of funding raised by the levy will be spent on social care in England.

**Market Sustainability and Fair Cost of Care Fund**

3.5.42 The provisional LGFS announced this new grant for 2022-23 intended to help local authorities to prepare their markets for reform and move towards paying the fair cost of care. The government has distributed funding using the adult social care relative needs formula and the 2022-23 allocation for Tower Hamlets was £0.989m. The budget allocated this funding in full to the Health, Adults and Community directorate.

3.5.43 Local authorities will be expected to carry out activities including:

- Conduct a cost of care exercise to determine sustainable rates.
- Engage with local authorities to improve data on operational costs and the number of self-funders.
- Strengthen capacity to plan and implement greater market oversight.
- Use the funding to increase fee rates (appropriate to local circumstances).

3.5.44 The grant is forecast to increase to circa £8.5m in 2023-24. The allocation of the budget to services is still to be determined, however it is envisaged that this will primarily be required to reduce adult social care client contribution income budgets (due to the cap on care costs) and to fund administration costs for the recording and monitoring of care costs paid and development of the market (e.g., commissioning/brokerage, accountancy, financial assessments and debt monitoring).

**Services Grant**

3.5.45 In the provisional LGFS, the Government introduced a one-off 2022-23 Services Grant and the allocation for Tower Hamlets was £7.688m. This grant was not ringfenced, and conditions on reporting requirements were not attached. It was provided in recognition of the vital services, including social care, delivered at every level of local government and also includes funding for local government costs for the increase in employer National Insurance Contributions.

3.5.46 The Government stated a clear intention for this grant to be one-off for 2022-23 but intend to work closely with local government on how to best use this funding from 2023-24 onwards. This funding would be excluded from any proposed baseline calculation for transitional support as a result of any proposed system changes but the funding could be used by Government to provide transitional relief from decreases in funding caused by the New Homes Bonus, Fair Funding Review and the Business Rates Reset.

**Public Health Grant**

3.5.47 The Public Health grant is ring-fenced for use on public health functions exclusively and covers all ages. The final allocation of the Public Health grant to Tower Hamlets for 2022-23 was £37.372m. The MTFS currently assumes inflationary increases for future years.

**Rough Sleeping Initiative**

3.5.48 The Rough Sleeping Initiative fund was created to provide local support for those living on the streets. This was first announced in March 2018 to make an immediate impact on the rising levels of rough sleeping. This funding combined the Rough Sleeping Initiative and Rapid Rehousing Pathway into a single, streamlined funding programme.

3.5.49 The budget estimates that the Council will receive an allocation of £0.646m in 2022-23 (allocation still to be announced) with the funding allocated directly to the Place directorate.

**Homelessness Prevention Grant**

3.5.50 The Flexible Homelessness Support & Homelessness Reduction grant was designed to transform the way councils fund homelessness services to provide greater flexibility to prioritise the prevention of homelessness. The grant empowers the Council to support the full range of homelessness services.

3.5.51 The government created a newly named Homelessness Prevention Grant that replaced the Flexible Homelessness Support and Homelessness Reduction grant in 2021-22. The new allocation for 2021-22 was £5.852m which was a

£0.746m increase on the previous grant. The MTFS includes this new grant allocation and assumes that this level will continue in future years with added inflation, with the funding allocated directly to the Place directorate to support services relating to homelessness in the borough.

**Local Tier Services Grant**

3.5.52 The Lower Tier Services Grant was introduced in the 2021-22 LGFS, intended to be “minimum floor funding” to ensure that no district or unitary council had a decrease in Core Spending Power for 2021-22. The government made it clear that “This funding is in response to the current exceptional circumstances and is a one-off. No local authority should take this funding floor as guaranteeing similar funding floors in future years, including in future finance reforms”.

3.5.53 The provisional LGFS retained the Lower Tier Services Grant for another year (2022-23) and the final LGFS confirmed the 2022-23 allocation for Tower Hamlets as £1.508m.

3.5.54 In 2021-22 the funding was placed into the Collection Fund Smoothing Reserve, to support the impact of the Covid-19 pandemic on Business Rates and Council Tax income. The 2022-23 budget utilised the one-off income to contribute to in-year funding of the Council’s expenditure and the MTFS currently assumes that this will continue in future years.

## 3.6 BUDGET PRESSURES, GROWTH AND INFLATION

3.6.1 A key part of the annual budget setting process is the review of growth pressures across the MTFS period arising from demographic changes, new requirements or responsibilities or inflationary pressures.

3.6.2 In previous budget setting processes, the Council approved amounts for unavoidable growth and estimated inflation over the period to 2023-24. These have been reviewed as part of updating the MTFS for the period until 2026 and in the context of the overall funding pressures and in particular as a result of the current high inflation rate and continuing impact of Covid-19.

3.6.3 In line with this review methodology, previously agreed demographic growth funding for Adult Social Care (ASC) in 2021-22 and 2022-23 was revised downwards to take account of a range of demand management measures that include more effective price controls to mitigate pressures (£3.5m revised growth for 2022-23). This was a risk-based proposal given the Council’s overall financial gap and given that the service is currently experiencing financial pressures on care packages. The 2022-23 budget allocated funding from the ASC Precept to support ASC demography (£1.2m). The MTFS includes allowance for further adult social care demographic growth pressures of circa £5.4m for each of 2023-24 to 2025-26, of which circa £4m per annum would be funded through growth and circa £1.4m per annum would only be provided if the 1% ASC Precept was allowed by government and agreed by Council to be implemented. The demography provision for ASC will need to take account pf the government's ASC Reform and potential funding to be provided from the new health and social care tax.

3.6.4 The Council remains part of the National Joint Council (NJC) for Local Government Services for negotiating pay award arrangements. The 2020-21 pay inflation was agreed nationally at 2.75% and the 2022-23 budget ensured that pay inflation was provided for this higher increase. The 2021-22 pay award has been agreed at 1.75% for most officers (2.75% for officers on the lowest spinal point and 1.5% for Chief Officer grades) in line with the budget provided for in the MTFS (which was based on a 1.75% average assumption).

3.6.5 The pay inflation requirement for 2022-23 was previously estimated at £3.8m, based on a 2% annual pay award and increased to provide for the recent bringing inhouse of IT and waste collection services. The 2022-23 budget also included a £1.4m allowance for the increased employer's NI contribution for the health and social care tax, funded in 2022-23 through the new Services Grant from Government. It is proposed in the MTFS refresh for the pay award allowance for 2022-23 to be increased to 4% and 4% also allowed for 2023-24, due to cost of living pressures on national negotiations, before returning to a 2% assumption for 2024-25 and 2025-26.

3.6.6 The refresh of the MTFS has also considered the currently heightened inflationary risks in non-pay inflation. Some large contracts include inflationary uplifts based on the Retail Price Index (RPI) or Consumer Price Index (CPI), which could be high in certain months following the recovery from the pandemic and the markets are experiencing pressures in areas such as labour and fuel which could affect the cost of new contracts. The year-on-year RPI increase for April 2022 is 11.1% and the CPI increase is 9.0%.

3.6.7 The 2022-23 budget allowed for non-pay inflation of 2.5%, slightly higher than the historic allowance of 2% based on the Bank of England's target rate. The refreshed MTFS proposes to increase this to 4.5%, provide 6% for 2023-24 and 4% for 2024-25, then returning to 2% for 2025-26.

3.6.8 The GLA will announce the London Living Wage (LLW) increase for 2023-24 around October. The Council is committed to fund social care homecare providers for any LLW increase as part of the Ethical Care Charter.

3.6.9 Directorates in the Council will further review their service areas over the summer for unavoidable growth and budget pressures that would be requested to be funded in 2023-26. Pressures that are currently known have been included in the proposals listed together with inflation, demography and changes to savings and core grants in Appendix 5. The MTFS currently assumes that the growth amounts previously indicated for 2023-24 and 2024-25, when the 2022-23 budget was set, will now be agreed in the 2023-26 budget.

## 3.7 SAVINGS PROPOSALS

### Savings Proposals – General Fund

3.7.1 The Council has previously approved savings to ensure that a balanced budget was in place for the MTFS three year period. However, amid considerable uncertainty around future funding levels, there remains an estimated budget gap for 2023-24 and 2025-26.

3.7.2 The Council will need to consider its strategy for meeting the budget gap going forward as part of budget setting for 2023/24.

3.7.3 The Council has previously approved savings totalling £7.181m in 2023-24. However, with the latest estimated significant budget gaps in both 2023-24 and 2024-25, there is a likely future need to identify significant additional savings for these years and to ensure all previously approved savings remain deliverable. Previously approved savings for 2023-24 will be reviewed by the current administration and are therefore subject to change. Detailed consultation and impact assessments will continue to be undertaken as the proposals agreed previously are taken through to implementation and the services will continue to develop and consult on proposals for future years.

3.7.4 The previously approved savings include increased fees and charges income for the Council of £0.235m in 2023-24, in line with results from the 2021 budget consultation which indicated support for an increase in income generation. The fees and charges report will be presented to Cabinet for agreement later in the financial year.

### Prior year savings to be written off - £2.200m

3.7.5 Following a robust review, the following previously agreed savings are considered to be no longer deliverable and it is proposed in this budget that these are now formally written off: -

- **Contract Management Efficiencies ref: SAV / CORP 02 / 18-19 £1.950m.** The current inflationary pressures on contract negotiations and procurements have resulted in these further contract efficiencies not being achievable.
- **Income Through Housing Companies ref: SAV/ RES 08 / 18-19 £0.250m.** There is currently no activity within the housing companies and a review of the use of the housing companies is being undertaken with a view to having a clear strategy around their roles and any savings that could be delivered.

### Re-profiled savings to later financial year - £0.100m

3.7.6 The following previously agreed savings are considered to be no longer deliverable within the originally planned timescales and it is proposed in this budget to re-profile these to following years;

- **THH - Potential support service savings ref: SAV / COP 002 / 21-22 £0.100m re-profiled from 2023-24 to 2025-26**. This saving relates to support service savings from the in-sourcing of THH and is therefore proposed to be re-profiled to allow time for the consideration of potential in-sourcing.

3.8 **RISKS AND OPPORTUNITIES**

3.8.1 When setting the draft MTFS, Service Directors have provided their best estimate of their service costs and income based on the information currently available to them. However, there will always be factors outside of the Council's direct control which have the potential to vary the key planning assumptions that underpin those estimates.

3.8.2 There are a number of significant risks that could affect either the level of service demand (and therefore service delivery costs) or its main sources of funding. In addition, there are general economic factors, such as the level of inflation and interest rates that can impact on the net cost of services going forward.

3.8.3 Pressures in service demand are demonstrated in the Council's budget monitoring for 2021-22, especially for children's and adult social care. The Council commissioned an external review of adult social care budgets, demography projections and savings plans. Consideration of the review and identified risks will feed into the medium-term financial planning process.

3.8.4 Similarly, there are opportunities to either reduce costs or increase income which will not, as yet, be fully factored into the planning assumptions. The main risks and opportunities are summarised below.

**Risks**

**Inflation**

- CPI Inflation rose to 9% in April 2022 and high inflation expected to persist throughout this financial year, driven largely by energy and goods prices. Rises in commodity prices, increases in shipping costs and supply shortages have together pushed up goods prices globally and reflected in UK import prices.
- Currently CPI is expected to return to a lower level over the medium term. However, there are impacts on Council budgets in relation to higher costs, greater demand for services and lower income collection as households face pressures associated with increased prices.

**Covid-19 Pandemic**

- Public health and wellbeing – both residents and staff
- Increase in service demand – especially mental health, social care, homelessness, unemployment and domestic abuse
- Increased levels of financial hardship, with poverty exacerbating existing inequalities
- Economic impact on Council funding
    - Potentially significant decreased business rates and council tax income levels; it will be vital for the Council to continue to receive government support for these reduced income levels
    - Decreased sales, fees and charges income

**Impact of decision to leave European Union (Brexit)**

- Workforce impact arising from direct or indirect employment of EU nationals.
- Supply chains are affected by changes in import and procurement legislation, and there are potential cost implications associated with currency fluctuations.
- The implications for pension funds are mixed as global investment vehicles have already priced in much of the uncertainty, but valuations on balance sheets and the cost of borrowing may lead to greater vulnerability.
- Commercial strategies may need to take into account the potential for any downturn in demand for properties in their investment portfolios which impact rental income and profitability.

**Regulatory Risk**

- **Business Rate Reset** – A proposed business rates reset by the Department for Levelling Up, Housing and Communities (DLUHC) means that the baseline level will be raised to the current level of business rates, and therefore Tower Hamlets will only retain extra income for growth that occurs above the new baseline expected level.
    - The target business rates amount since 2013-14 was set on cash amounts received in previous years. This created winners and losers depending on the timing of appeals. Tower Hamlets benefited from the methodology chosen, plus has benefitted from growth achieved locally since 2013-14.
    - It was always DLUHC's intention to update the target amounts. This was planned to take place in 2019-20 but has been delayed until at least 2023-24, so, in this regard, Tower Hamlets has benefitted. It is envisaged that resets will also occur periodically going forward.
    - Once the reset takes place, the growth will be redistributed based on need (within the funding formula) and Tower Hamlets will receive a share. Tower Hamlets should also receive more resources going forward, if local growth continues.

- **Review of relative needs and resources (also called the Fair Funding Review) -** The government has committed to reforming the way local authorities are funded. Its Fair Funding Review aimed to introduce a new funding formula from April 2021, now delayed to at least April 2023. The government has said that the Fair Funding Review will: -

    - set new baseline funding allocations for local authorities;
    - deliver an up-to-date assessment of the relative needs of local authorities;
    - examine the relative resources available to local authorities;
    - focus initially on the services currently funded through the local government finance settlement;
    - be developed through close collaboration with local government to seek views on the right approach.

  - It is considered likely that London authorities will be adversely affected by the changes and it is therefore sensible to plan for a variation in funding levels even after allowing for transitional arrangements.

**Adult Social Care Services**

- **Price pressures in the social care market** – impact of workforce shortages and inflation on labour, fuel, food and clothing costs.
- **Discharge from hospital** – reduction in NHS funding for the short-term funding of care costs for residents that are discharged from hospital.
- **Long Covid** – the long term effects on the health and social care needs of residents are unclear and may increase demand for community and residential based services.
- **National implementation of a care cap on client contributions** – reduction in income and an increase in administration costs (updating the calculations of contribution levels and monitoring of contributions paid against the cap which will also include self-funders).

**General Economic Factors**

- Economic growth slowing down or disappearing
- Reductions in grant and third party funding
- Reductions in the level of income generated through fees and charges
- A general reduction in debt recovery levels
- Increase in fraud

**Increases in Service Demand**

- Adult Social Care homecare and residential care services

- Children's Social Care including an increase in the number of looked after children, unaccompanied asylum seekers or those with no recourse to public funds
- Housing (including homelessness and temporary accommodation)
- General demographic trends (including a rising and ageing population)
- Impact of changes to Welfare Benefits

**Efficiencies and Savings Programme**

- Non-delivery of savings remains a key risk to the Council and will continue to be monitored during the current and next financial year
- Slippage in the expected delivery of the savings programme

**Opportunities**

- Growth in local taxbase for both housing and businesses
- Service transformation and redesign including digital services
- Invest to save approach (including capital improvements) to reduce revenue costs
- Income generation opportunities including through a more commercial approach

## 3.9 RESERVES

3.9.1 Reserves are an important part of the Council's financial strategy and are held to create long-term budgetary stability. They enable the Council to mitigate future risks, such as increased demand and costs; to help absorb the costs of future liabilities; and to enable the Council to resource policy developments and initiatives without a disruptive impact on rates of Council Tax.

3.9.2 The Council's key sources of funding face an uncertain future and the Council, therefore, holds earmarked reserves and a working balance in order to mitigate future financial risks. There are two main types of reserves:

- Earmarked Reserves – held for identified purposes and are used to maintain a resource in order to provide for expenditure in a future year/s.
- General Reserves – these are held for 'unforeseen' events.

3.9.3 The Council maintains reserves for its General Fund activities, in respect of its Housing Revenue Account (HRA) and for Schools. Capital reserves are also held to support funding of the Council's capital investment strategy.

3.9.4 The amount of reserves held is a matter of judgment which takes into account the reasons why reserves are maintained and the Council's potential financial exposure to risks. The Council's current Reserves Policy is included in Appendix 7. Reserves are one-off funds and, therefore, the Council should always aim to avoid using reserves to meet on-going financial commitments other than as part of a sustainable budget plan. In the current unprecedented challenging environment, it is even more important to ensure reserves are maintained and not on a continuing declining trajectory. The level of General

Revenue balance is maintained at the level agreed in the Financial Regulations of the Council, currently £20m.

3.9.5 Reserves are therefore held for the following purposes:

- Providing a working balance i.e. Housing Revenue Account and General Fund.
- Smoothing the impact of uneven expenditure profiles between years e.g. collection fund surpluses or deficits, local elections, structural building maintenance and carrying forward expenditure between years.
- Holding funds for future spending plans e.g. capital expenditure plans and for the renewal of operational assets e.g. information technology renewal.
- Meeting future costs and liabilities where an accounting 'provision' cannot be justified.
- Meeting future costs and liabilities so as to cushion the effect on services e.g. the Insurance Reserve for self-funded liabilities arising from insurance claims.
- To provide resilience against future risks.
- To create policy capacity in a context of forecast declining future external resources.
- The use of some reserves is limited by regulation e.g. reserves established through the Housing Revenue Account can only be applied within that account and the Car Parking reserve can only be used to fund specific transport related expenditure. Schools reserves are also ring-fenced for their use.

3.9.6 An overview of reserves are presented below (subject to completion of outturn and audit completion of the statement of accounts)

| **Reserves Summary** | **Forecast 31/03/22** |
|---|---|
| | **£m** |
| General Fund Reserve | 23.8 |
| | |
| Earmarked Reserves with Restrictions on use | 120.7 |
| Earmarked Reserves without Restrictions | 86.5 |
| **Total Forecast General Fund Earmarked Revenue Reserves** | **207.2** |
| | |
| **Other Reserves** | |
| Housing Revenue Account | 52.5 |
| Schools Balances | 36.5 |
| Dedicated Schools Grant Surplus / (Deficit) | (10.6) |
| | |
| **Reserves restricted by law to finance Capital Expenditure** | |
| Capital Grants Unapplied | 192.7 |
| Capital Receipts Reserve | 128.3 |
| | |

| | |
|---|---|
| **Overall Reserves Total** | **630.4** |

## 3.10 SCHOOLS' FUNDING

3.10.1 The largest single grant received by the Council is the Dedicated Schools Grant (DSG), which is ring-fenced to fund school budgets and services that directly support the education of pupils. The Local Authority receives its DSG allocation gross (including allocations relating to academies and post 16 provision), and then the Education & Skills Funding Agency (ESFA) recoups the actual budget for Academies to pay them directly, based on the same formula as the funding allocations made to Tower Hamlets maintained schools. This leaves a net LA cash budget.

3.10.2 The DSG is allocated through four blocks: The Schools Block, Central School Services Block, High Needs Block and Early Years Block. All elements of the DSG are calculated based on a national funding formula, however these are calculated using historic funding as a baseline.

3.10.3 Whilst the Schools Block allocation for 2022-23 is based on allocating a school level budget calculation, the method of distribution to schools is still through a local formula methodology.

3.10.4 In December 2021 the ESFA published initial allocations for 2022-23 for the Schools Block, Central Services Block High Needs Block and the Early Years block. The allocations for the High Needs block and the Early Years block are further updated in year in line with pupil data changes whilst the Schools Block and Central School Services block are final allocations.

3.10.5 The Early years block is based on pupil take up on an hourly rate which is £8.06 per hour for 3 and 4 year olds and £6.87 per hour for 2 year olds. Tower Hamlets rate has been frozen for 3 and 4 year olds for the last three years with only the 2 year old rate increased by 21p or 3.1% for 2022-23. The initial Early Years Block allocation is based on January 2021 early years numbers which were lower than in previous year due to the Pandemic, we would expect the final allocation to be increased for actual pupil take up.

3.10.6 Additional funding for Pupil growth in the Schools Block for 2022-23 has been included in the December allocation at £1.796m this is calculated using growing pupil numbers in Middle Super Output Areas between October 2020 and October 2021 ignoring reductions in other areas. This methodology benefits Tower Hamlets with the movement in demand across the borough plus we have seen an increase in total pupils from the previous year of 597 or 1.6%.

3.10.7 The Schools block of the DSG has increased by 2% per pupil for 2022-23, whilst the overall cash increase is 4% this relates to the growth in the pupil population.

3.10.8 The High Needs Block is funding to support costs of pupils with additional education needs, across mainstream and special schools as well as the associated support costs. The allocation of the high needs block for 2022-23 has increased by 8%, which will go some way to ease the pressure on current spend and mean we are able of manage the high needs block spend within the financial year as well as build additional capacity. However, there continues to be an accrued deficit that will be bought forward and can, in line with government guidance, be bought back into balance over a number of future financial years.

3.10.9 Significant work continues to take place to identify efficiencies in high needs provision, including remodelling of central services, review of top ups paid to individual schools as well as building local capacity to prevent expensive placements outside of LBTH. A long term management plan for high needs will be reviewed with the Department for Education in 2022-23.

3.10.10 The Central Schools Services Block (CSSB) was introduced in 2018-19 to fund LAs for their statutory duties relating to maintained schools and academies. The CSSB brings together funding previously allocated through the retained duties element of the Education Services Grant (ESG) funding for ongoing central functions e.g. admissions and funding for historic commitments including items previously agreed locally such as contributions to central Education budgets.

3.10.11 As part of the national funding formula the DfE are reducing the allocation within the CSSB of historic commitments and therefore the CSSB for Tower Hamlets has been decreased by £376k in relation to historic commitment for 2022-23.

3.10.12 In addition to the Central Schools Services Block, maintained schools can, through the Schools Forum, agree to de-delegate some of their Schools Block resources for certain specific services that schools would benefit from the economies of being managed centrally. Schools can also make contributions to support the former Education Services Grant (ESG) general duties which was removed as a separate grant in 2017. This contribution supports costs the Council is obliged to carry out as statutory duties for maintained schools, for example in relation to financial regulation, asset management, internal audit, HR and the provision of information to government departments and agencies. Schools Forum were asked at the School Forum of 12th January 2022 to increase these contributions and de-delegations by 2% to match the increase in the schools. These rates were agreed for one year only and will need to be reviewed in October for 2023-24.

3.10.13 The table below sets out the DSG allocation over the funding blocks for 2022-23. Please note that the 2022-23 allocations will be finalised in July 2022.

**Dedicated Schools Grant – Initial 2022-23 and Final 2021-22**

| Block<br>Gross | 2022-23<br>£m | 2021-22<br>£m | Change<br>£m |
|---|---|---|---|
| Schools Block | 289,896 | 278,633 | 11,263 |
| CSSB | 3,511 | 3,887 | (376) |
| High Needs Block | 71,875 | 65,820 | 6,055 |
| Early Years Block | 27,927 | 31,139 | (3,212) |
| **Total** | **393,209** | **379,479** | **13,730** |

3.10.14 In addition, the Council receives, and passports fully to schools, funding for the pupil premium (£20.9m in 2021-22) and sixth form funding (circa £13m). Final allocations for the pupil premium will be confirmed in July 2022 and sixth form funding in March 2022. In 2021-22 a number of Covid related catch up funds were also passported fully to Schools which have yet to be confirmed as continuing into future years. Schools will receive a supplementary grant for 2022-23 to cover the health and social care NI tax and for other cost pressures.

**Tower Hamlets' Funding Formulae**

3.10.15 The agreement on the local Schools Funding Formula and Early Years Funding Formula is a decision for the Council following consultation with the Schools Forum. Schools Forum have agreed to mirror the national funding formula which was confirmed in the January Forum meeting, and is line with the direction of travel stated by government. Schools Forum will consider the following:

- That the National Schools Funding Formula (NSFF) adopted by Tower Hamlets originally in 2019-20 continues for 2023-24.

- That the Minimum Funding Guarantee (the mechanism that guarantees schools a minimum uplift in per-pupil funding) would be set at the maximum allowed.

- That the structure of the Early Years Funding Formula remains unchanged.

3.11 **HOUSING REVENUE ACCOUNT (HRA)**

3.11.1 The Housing Revenue Account (HRA) relates to the activities of the Council as landlord of its dwelling stock. Since April 1990 the HRA has been “ring-fenced”. This means that any surplus or deficit on the Housing Revenue Account cannot be transferred to the General Fund. The HRA must also remain in balance.

3.11.2 From April 2012, the HRA subsidy grant was abolished and replaced by self-financing, under which local authorities retain all rental income, but are responsible for meeting all costs relating to Council housing.

**2022-23 Rent Increase**

3.11.3 Section 23 of the Welfare Reform and Work Act forced local authorities to implement a rent reduction of 1% for four years starting in 2016-17. The last year to which the rent reduction applied was 2019-20.

3.11.4 In September 2018 the government published a consultation entitled ‘Rents for social housing from 2020-21’ in which it set out its proposals for social rent policy from 2020-21. The proposals are that the Regulator of Social Housing’s rent standard will, from 2020-21, apply to local authorities. This will mean that, in common with other Registered Providers (RPs), local authorities will be permitted to increase their rents by a maximum of CPI + 1% for at least five years.

3.11.5 Any rent increase is based on the September CPI figure, and therefore the maximum rent increase would be CPI +1%. In 2022-23 the increase was 4.1% (CPI of 3.1% plus 1%). The table below shows the impact on rental income by bedroom size:

| Bedroom Numbers | 2015-16 Average Weekly Rent | 2021-22 Average Weekly Rent | 2022-23 Average Weekly Rent | £ Weekly Increase (21-22 to 22-23) |
|---|---|---|---|---|
| 0 Bed | 85.49 | 85.81 | 89.33 | 3.52 |
| 1 Bed | 99.28 | 99.32 | 103.39 | 4.07 |
| 2 Bed | 112.17 | 112.27 | 116.87 | 4.60 |
| 3 Bed | 126.06 | 126.48 | 131.67 | 5.19 |
| 4 Bed | 141.35 | 143.36 | 149.24 | 5.88 |
| 5 Bed | 156.97 | 156.19 | 162.59 | 6.40 |
| 6 Bed | 160.34 | 160.06 | 166.62 | 6.56 |

The 2022-23 rent increase was the first year in which rent levels have risen above 2015-16 rents prior to the enforced rent cuts detailed in para. 3.11.3

3.11.6 Within the formula rent calculation there is the ability to charge up to 5% more on the base rent levels for specific reasons, for example, a new build council house. This flexibility has not been applied in Tower Hamlets to date.

**2022-23 Increase in Tenanted Service Charges**

3.11.7 LBTH should budget to recover the cost it incurs on providing services to tenants through the service charge made to them. Historically these charges have been subject to an inflationary increase, with the assumption being that the cost of providing the services will incur an annual inflationary increase. As a result, the 2022-23 tenanted service charges were increased by 3.1% (September CPI figure).

3.11.8 The table below details the current service charges and the impact of the 2022-23 3.1% CPI inflationary increase.

| Service Charge | 2021-22 Average Weekly Charge | 2022-23 Average Weekly Charge | £ Weekly Increase (21-22 to 22-23) |
|---|---|---|---|
| Block Cleaning | 5.70 | 5.88 | 0.18 |
| Estate Cleaning | 2.50 | 2.58 | 0.08 |
| Concierge | 9.97 | 10.28 | 0.31 |
| Horticulture | 0.81 | 0.84 | 0.03 |
| ASB | 1.20 | 1.24 | 0.04 |
| Boiler Fuel | 14.28 | 14.72 | 0.44 |
| Communal Energy | 1.33 | 1.37 | 0.04 |
| Total | 35.79 | 36.91 | 1.12 |

**Repairs and Maintenance**

3.11.9 The 2021-22 repairs and maintenance budget included a growth item of £250k for a five-year programme of electrical testing. The 2022-23 budget was increased by a 5% inflationary increase. The level of inflationary increase for 2023-24 will need to consider the currently higher level of inflation, especially in labour and material costs resulting from Brexit, the pandemic and the current cost of living pressures.

3.11.10 The main repairs and maintenance contract, currently with Mears is planned to be re-procured during the year. As a result the future cost of providing the service is unknown at this stage.

**Energy**

3.11.11 The 2021-22 energy budget was held at the same level as the previous year with no inflation applied following a new energy contract being procured. However, wholesale gas and power markets have been extremely volatile since December 2020, with prices recently hitting a new decade high. It is uncertain whether this is a short-term increase or a more long-term fundamental change to the UK energy prices but it is likely to impact on the cost of energy and will need to be factored into the MTFS and annual HRA budgets.

3.11.12 Tower Hamlets exposure to these price increases has been partially mitigated in recent years through the pre-emptive step to hedge most of the energy required. However, the longer-term impact will affect prices and the impact on the 2023-24 budget is being evaluated. An inflationary rise has been applied to the energy budget for 2022-23 however current market prices present a pressure to the HRA.

**Management Fee**

3.11.13 The Management Fee represents the largest single expenditure element of the HRA budget. In March 2022, Council approved the 2022-23 Management Fee payable to THH for services provided to the Council at £33.236m. This has increased by £0.440m to £33.676m following the agreement of the 2021-22 NJC national pay award.

3.11.14 The table below shows the calculation of the 2022-23 Management Fee payable to THH.

**Calculation of 2022-23 Management Fee**

| Description | Total £m |
|---|---|
| **Management Fee 2021-22** | 32.615 |
| Add: 2021-22 Pay Award | 0.440 |
| Savings from Salary and Non-Salary Budgets | (0.313) |
| Growth from Non-Pay related activities | 0.075 |
| Growth from Pay related activities | 0.217 |
| Growth - Building Safety | 0.642 |
| **Management Fee 2022-23** | **33.676** |

3.11.15 The 2022-23 management fee does not include an inflationary increase in relation to the 2022-23 NJC pay award which is still to be agreed nationally. Salary costs represent approximately £20m of the management fee and any formally agreed increase will need to be reflected in the 2022-23 management fee.

**Savings**

3.11.16 At its meeting on 26th July 2016, the Mayor in Cabinet agreed a HRA medium-term savings target of £6m. The budget for 2021-22 represented the final £1m tranche of this saving, with £5m already having been delivered across the management fee and delegated budgets.

3.11.17 Following the delivery of £6m of savings over the previous five years, THH indicated that it was difficult to deliver significant savings in 2022-23 without cutting services. It was therefore agreed to implement a negligible savings target in 2022-23, with larger targets in following years once THH move to the New Town Hall and can take advantage of the synergies that this will bring.

3.11.18 As part of its budget setting process, THH identified £0.313m of savings that were deliverable against the management fee in 2022-23. Staff savings of £0.042m were identified, primarily from the re-organisation of the Business Development Team to enable the creation of a Regulatory Assurance Team. The remaining £0.271m of savings related to non-staffing budgets following service reviews, new ways of working following on from the pandemic and in preparation to moving to the new Town Hall. The savings also included budgets that had not been utilised and for which no plans were in place for its use.

**Growth – Management Fee**

3.11.19 In 2022-23 a new permanent growth item was agreed totalling £0.642m to ensure that the Council is meeting its obligations for building and fire safety following the Hackett review. The growth has funded the appointment of a team comprising a Fire Safety Manager and eight Building Safety Officers.

3.11.20 The Fire (Building) Safety Manager will be the Council's 'named individual' and will manage our programme of fire risk assessments, EWS surveys and Type 4/compartmentation surveys; ensure compliance with the requirements of PAS9980 which relates to the holistic risk assessment of external walls; manage as part of the wider team the building safety officers who will primarily focus on our portfolio of 69 high rise buildings; inform the investment programme and help us to understand our priorities and provide advice within the organisation and support the project managers and delivery of fire safety remedial works.

3.11.21 The Building Safety Officers (seven Officers and one Senior) will manage all 69 high rise buildings over 6 stories and other buildings as may be deemed appropriate; each officer will have a portfolio of 10 buildings and they will be the public face with all residents in those buildings and lead resident engagement strategies; lead on enforcement action in relation to all fire safety issues (inc. leaseholders) i.e. gates/grills etc; work with suitable 3rd parties in ensuring that all front entrance doors across the 3966 flats in the 69 high rise buildings meet the relevant standard. This includes 1353 leaseholders; have a high profile in each building and carryout regular inspections working with caretakers.

3.11.22 A further £0.217m of pay related growth related to the recruitment of additional caretakers for new build properties; the realignment of gardener's salaries as agreed with trade unions and overtime payments for ASB officers when providing an out of hours text service.

3.11.23 Non-pay growth of £0.075m related to an increase in rent paid on a property following a rent review, software upgrade for the Health & Safety system and training for the new building safety team.

**Growth – HRA Delegated Budgets**

3.11.24 A further permanent growth bid of £356k was agreed relating to the clienting of the building safety bill. This growth was split over two years, with £108k required in 2022-23 and the remainder in 2023-24.

3.11.25 The Building Safety Bill introduces a new regime applicable to all high-risk/high-rise buildings that are 18 meters or 7 storeys and more in height with two or more residential units. This includes our existing housing stock, new developments that are ready for residents to move into and some commercial units located on the ground floor of residential blocks in scope of the Bill.

3.11.26 The Bill will improve the fire and structural safety of new and existing residential buildings and focuses on accountability at each stage of a building's lifecycle. Non-compliance with the Building Safety Act could result in fines and/or imprisonment.

3.11.27 The Council is required to undertake building safety case reviews with a requirement to complete intrusive external wall system surveys to the blocks managed by THH of 7+ storeys or 18m+. This represented a new requirement with costs estimated at £0.353m agreed as growth.

3.11.28 It was also agreed to increase the feasibility budget within the HRA by £1.5m to support the new build housing capital programme, enabling the continued identification of sites, develop designs, carry out cost and viability appraisals and proceed towards planning applications for the delivery programme.

3.11.29 The contracts for asbestos surveys, fire risk assessments and stock conditions surveys have been awarded and the procurement for water risk assessments has been relet. The overall 4-year budget for each contract was agreed resulting in growth of £0.783m.

**Overall position on the HRA**

3.11.30 The HRA business plan will be refreshed as part of 2023-26 budget setting to model the impact of the risks and opportunities detailed above to assess that the key parameters within which it operates will not be breached. These include HRA reserve balances maintained at a minimum of £10m and an Interest Cover Ratio (the number of times rental income can cover interest repayments on borrowing) above 1.5.

**Update on Government Policies Affecting the HRA**

3.11.31 There have been a number of recent government consultations and announcements and these are outlined below.

**Social Housing White Paper**

3.11.32 In November 2020 the Government issued its social housing white paper - The charter for social housing residents, with a focus on tenant safety, consumer protection and redress. The Regulator of Social Housing (RSH) has been tasked with setting up a new consumer regulatory function which will proactively monitor and ensure compliance with updated consumer standards

3.11.33 The removal of the 'serious detriment' test along with the introduction of both routine and reactive inspections for all landlords with more than 1000 homes signals a new approach to consumer regulation with implications for the way councils manage the ALMO relationship and gain assurance, providing the regulator with greater oversight of the performance of the local authority landlord function' emphasising that where management has been contracted out to an ALMO or TMO, it is the local authority as landlord that is responsible for meeting the regulatory standards.

3.11.34 This brings a renewed focus on the client role and how the local authority gains assurance. Councils will need to demonstrate to the regulator how they know the ALMO is performing and ensure there are robust measures in place to ensure compliance with the consumer standards and a shift towards more contractual compliance and the White Paper suggests councils should review their contracts to ensure they do not hinder the RSH in the exercise of its powers.

3.11.35 Landlords will also be required to specify a named 'responsible person for Consumer Standards' and a named 'responsible person for health and safety'. It is unclear whether it will be possible to delegate these roles to the ALMO, however the likelihood is that the Regulator will follow the precedent set in the Building Safety Bill which requires the landlord to undertake the Authorised Person role directly.

3.11.36 The White Paper also introduces new requirements in terms of landlord transparency and accountability to tenants. The regulator is tasked with developing arrangements to collect and publish a core set of tenant satisfaction measures for all social landlords so tenants will know how their landlord is performing relative to others in the sector. Whilst operationally much of this will be delegated to the ALMO, LBTH will need to keep a close eye on all aspects of performance including complaints and satisfaction levels with different aspects of the services.

**Building Safety Bill**

3.11.37 The government is bringing forward fundamental changes in the draft Building Safety Bill that will improve building and fire safety, so that people will be, and will feel, safer in their homes following the Grenfell Tower fire.

3.11.38 Dame Judith Hackitt carried out an independent review of building regulations and fire safety to understand the causes of the fire. The review concluded that the whole system needed major reform and that residents' safety needed to be a greater priority through the entire life cycle of a building – from design and construction, through to when people are living in their home.

3.11.39 The Building Safety Bill will sit alongside the recent Fire Safety Act 2021 was introduced on 5th July 2021 and has now recently received Royal Ascent, with full implementation in 2023.

3.11.40 Measures will be put place to make people safer in their homes. The Bill will ensure that there will always be someone responsible for keeping residents safe in high rise buildings – those 18 metres and above. They will also have to listen and respond to residents' concerns and ensure their voices are heard – they will be called the 'Accountable Person'.

3.11.41 Residents and leaseholders will have access to vital safety information about their building and new complaints handling requirements will be introduced to make sure effective action is taken where concerns are raised.

3.11.42 As announced in the Queen's speech on 11th May 2021, a new Building Safety Regulator will be established to oversee and make sure that Accountable Persons are carrying out their duties properly. The new Regulator will sit within the Health and Safety Executive and will have the power to prosecute property developers and landlords that do not meet safety standards as set out in the Bill.

3.11.43 The Regulator will work closely with duty holders both within the Council and THH throughout the lifecycle of Council owned stock and will ensure that high rise buildings and the people who live in them are being kept safe and will have new powers to raise and enforce higher standards of safety and performance across all buildings.

3.11.44 The draft Bill will make sure that those responsible for the safety of residents are accountable for any mistakes and must put them right. It will fully establish the regulator that will enforce new rules and take strong actions against those who break them.

3.11.45 The regulator will have 3 main functions: to oversee the safety and standard of all buildings, directly assure the safety of higher-risk buildings; and improve the competence of people responsible for managing and overseeing building work.

3.11.46 It will operate a new, more stringent set of rules for high-rise residential buildings. The new set of rules, contained in the draft Bill, will apply when buildings are designed, constructed and then later occupied.

3.11.47 At each of these 3 stages, it will be clear who is responsible for managing the potential risks and what is required to move to the next stage enabling a 'golden thread' of vital information about the building to be gathered over its lifetime.

3.11.48 When residents move into a building that falls under the new set of rules, it will need to be registered with the Building Safety Regulator and apply for a Building Assurance Certificate. The Accountable Person will need to conduct and maintain a safety case risk assessment for the building and appoint a Building Safety Manager to oversee it day to day.

3.11.49 The bill also bans the use of combustible materials on the external walls of high-rise buildings, publishes clearer guidance on existing regulations that buildings owners must follow, and will make it mandatory for sprinklers to be fitted in all new blocks of flats over 11 metres high.

**Fire Safety Act**

3.11.50 The Fire Safety Act 2021 received Royal Ascent in April 2021. Implementation arrangements will be set out in legislation, namely Regulations and associated guidance to be issued by the Home Office. The implementation timetable envisaged a commencement date of April 2022.

3.11.51 These regulations will place significant obligations on landlords of high-rise and multi-occupancy residential buildings, including:

- Requiring the Council to consider the spread of fire across external surfaces of its buildings. This means that priority will need to be given to implementing a programme of External Wall Surveys which will require significant internal resource and expertise. It is proposed that the new Fire Safety Manager will taking a leading role in this respect and manage the programme of inspections.
- The Fire Safety Act will also require front entrance doors and balconies to be included within the scope of fire risk assessments to ensure that they are in good condition and fit for purpose. This applies equally regardless of tenure and it is envisaged that the new building safety officers will play a key role in enforcing this.
- It is likely that the Act will require the Council to consider those residents who may need assistance in the event of the building being evacuated and put in place an appropriate plan (PEEP). Again, in high rise buildings the safety officers will lead on this.

The Act will empower fire and rescue services to take enforcement action and hold building owners to account if they are not compliant.

3.11.52 The Act provides a foundation for secondary legislation to take forward recommendations from the Grenfell Tower Inquiry phase one report, which stated that building owners and managers of high-rise and multi-occupied residential buildings should be responsible for a number of areas including:

- regular inspections of lifts and the reporting of results to the local fire and rescue services

- ensuring evacuation plans are reviewed and regularly updated and personal evacuation plans are in place for residents whose ability to evacuate may be compromised
- ensuring fire safety instructions are provided to residents in a form that they can reasonably be expected to understand
- ensuring individual flat entrance doors, where the external walls of the building have unsafe cladding, comply with current standards

**Removal of HRA debt cap**

3.11.53 The government announced in October 2018 that the HRA debt cap would be scrapped and this took effect from 29th October 2018. Removing the HRA debt cap means that instead of having a limit to the amount of debt that the HRA can undertake, HRA borrowing must – along with General Fund borrowing - be subject to the Prudential Code meaning that borrowing must be affordable, prudent and sustainable.

3.11.54 Under current rules, although interest charges on outstanding debt must be paid, the HRA has not made any provision for debt repayment in recent years. As non-repayment of debt is not sustainable over the long-term as it would result in increasing levels of interest charges being incurred, the s151 officer has decided that the charging of Minimum Revenue Provision (MRP) must be made to ensure the repayment of any borrowing is made over the usable lifespan of the assets, similar to the Minimum Revenue Provision (MRP) arrangements that operate for the Council's General Fund. If MRP is not charged, then future administrations will inherit ongoing debt costs that will be very difficult to reduce within budget constraints.

3.11.55 The s151 officer has also introduced a number of metrics within which the HRA must remain to ensure that borrowing levels remain prudent and interest / debt repayment remains affordable. These most important metric is a maximum interest cover ratio (the number of times LBTH can cover its interest payments from its income) of 1.5. This in effect places an artificial cap on the HRA as it limits the interest that can be repaid and therefore the amount borrowed. An ICR of 1.5 is in line with other similar Local Authorities and therefore deemed to be set at the right level.

**Social Rent policy 2019-20 onwards**

3.11.56 On 13th September 2018 the government published a consultation 'Rents for social housing from 2020-21' in which the government set out its proposals in relation to social rent policy from 2020-21.

3.11.57 In the consultation the government proposed that the Regulator of Social Housing's rent standard will:

i. permit Registered Providers (RPs) to increase their rents by a maximum of CPI + 1% for at least five years
ii. also now apply to Local Authorities

3.11.58 The government has now confirmed this policy and this means that in future local authorities will no longer have any discretion over their rent policy and will have to adhere to the Regulator's rent standard.

3.11.59 Historically local authorities have been able to make decisions on their rent policy with the only control mechanism being the annual 'Limit Rent', used to control Housing Benefit grant paid to the Authority by the Government.

3.11.60 With the introduction of HRA Self-Financing in April 2012, in return for being responsible for all items of expenditure and risk within the HRA, local authorities were meant to have discretion over their rent policy. As rent is the largest income stream within the HRA, having discretion over rent levels is seen as crucial in terms of running the HRA as a 'business'.

3.11.61 However, since 2012, the government has in relation to rents -:

- ended their rent restructuring policy a year early;
- implemented legislation to impose a 1% rent cut for four years;
- introduced the Regulator's rent standard to local authorities (as well as RPs) so that annual rent increases will be set out by the Regulator.

3.11.62 The most recent HRA 30 year financial modelling already assumes that after the four years of 1% rent cuts, HRA rents will increase by CPI + 1% for five years, and then by CPI only. The financial model set CPI at 3.1% for 2021-22 rent setting and assumes 2% throughout the remainder of the 30 year period.

**Right to Buy receipts**

3.11.63 The government's consultation on the use of right to buy receipts was launched in August 2018, reaching a conclusion in March 2021 with the publication of its consultation 'Use of receipts from Right to Buy sales'.

3.11.64 Original rules set out that Right to Buy 'one for one' receipts must be spent on replacement social housing within three years. Any unused receipts after three years were paid back, along with interest at 4% to MHCLG.

3.11.65 Under the new rules put forward by the Government in its Right to Buy consultation response, the timeframe local authorities have to spend new and existing Right to Buy receipts will be extended from three years to five years. This change has been backdated, and Councils will be able to apply this to receipts received as long ago as 2017-18 with the view that it will allow longer-term planning, including allowing larger plots of land to be remediated.

3.11.66 The response to the consultation also brought changes to the percentage cap that Councils can use on the construction of new homes, with the cap rising from 30% to 40% in a bid to make it easier for Local Authorities to fund replacement homes, particularly those for social rent. In Tower Hamlets, the cap has been applied at 30% to the existing housing programme and 40% to the future programme.

3.11.67 Authorities can use receipts to supply shared ownership and First Homes, as well as housing at affordable and social rent, to help them build the types of home most needed in their communities.

3.11.68 Right to Buy receipts for acquisitions will be capped to help drive new supply with effect from 1 April 2022 and phased in over 2022-23 to 2024-25. From April 2022 it will prohibit more than 50% of RTB replacements being delivered as acquisitions in financial year 2022-2023, reducing to 40% in 2023-24 and 30% from 2024-25 onwards.

3.11.69 Pooling of RTB receipts will take place annually, replacing the former quarterly system. Deadlines for spending retained receipts will also be calculated on an annual basis. A minimal amount of non-financial management information will still be collected quarterly.

**Risks – Welfare Reform**

3.11.70 The cumulative impact on the HRA will not be clear until the various reforms all take effect. Provision has been made within the HRA MTFP for an increase in bad debts but as the introduction of Universal Credit has been delayed it is not yet clear precisely what the future level of bad debts will be.

**Risks – Brexit and Cost of Living Inflation**

3.11.71 On 31 December 2021 the United Kingdom left the European Union. The house building industry is reliant on a significant number of EU workers and procuring materials from EU countries. As a result, there is a risk of delays to house building and costs increasing which will impact on the 30-year business plan and delivery of Government legislation and manifesto commitments.

3.11.72 The BCIS Price Adjustment Formula Indices for May 2021 shows the most significant cost increase is in materials. The highest increase is in the cost of structural steel which increased by more than 30% between May 2020 and May 2021 (Source: BCIS). Other increases are lower (e.g. cost of composite windows and doors increased by around 15%; hardwood fittings by 7%; ready mixed concrete and tile cladding by 3%), but will still have an impact on total scheme costs. Added to this, lead-in times for materials and components have lengthened resulting in delays in delivery and the associated increase in costs.

3.11.73 Rising labour costs, combined with shortage of skills in certain trades, is also having an impact on project costs and delivery timetables. Contractors who rely on sub-contractors rather than their own directly employed labour force are most affected. Some workers have left the industry permanently due to pandemic and post-Brexit immigration rules have resulted in a reduction in the pool of workers available for construction activity.

3.11.74 In addition to changes in market conditions, new Health and Safety rules including the Fire Safety Bill, Building Safety Bill and Construction and Design Management Regulations will add further cost to construction projects, as will the target of meeting net carbon zero by 2025.

3.11.75 Turner and Townsend estimate that tender prices will be inflated over the next three years, increasing from 1.5% in 2021 to 4.5% in 2024 for built product and from 2% in 2021 to 5% in 2024 for infrastructure projects. However, recent returns for projects in the capital programme tendered in the last three months have seen prices increase by up to 15% as a result of material, supply chain and labour costs. These cost increases will impact on affordability within the HRA business plan.

3.11.76 The current high level of inflation in the economy will have an impact on pay and non-pay budgets across the HRA and will be reviewed as part of the HRA business plan update.

**Risks – Covid-19 Pandemic**

3.11.77 On the 23rd March 2020 the UK entered into its first lockdown in response to the coronavirus pandemic. Since then, there have been two further lockdowns, with a phased ending of the third lockdown commencing on 8 March 2021. In total the UK has spent in excess of six months in lockdown restrictions. During this time many tenants have experienced hardship through the inability to work or loss of employment. Despite this, rent and service charge collection rates have remained stable and broadly in line with pre-pandemic levels. However, any further restrictions resulting from the pandemic could result in collection rates falling and an impact on the affordability of the HRA business plan.

## 3.12 CAPITAL

3.12.1 Council approved the 2022-25 capital programme of £347.282m for the General Fund programme and £411.927m for the Housing Revenue Account programme in March 2022. The capital programme was for a three-year period, with commitments beyond 2025 resulting from the current programme to be funded in future years. Capital expenditure is focussed on the council's strategic priorities.

3.12.2 The 2021-22 capital outturn, including details on slippage, is presented separately at today's Cabinet meeting. The capital programme is being refreshed for 2023-26 and will be presented, including any additions and changes to the programme, to a later Cabinet meeting for approval.

## 3.13 TREASURY MANAGEMENT STRATEGY

3.13.1 The Treasury Management Strategy Statement will be revised and agreed with Audit Committee in January 2023, and recommended for full Council approval in March 2023 in accordance with the CIPFA Treasury Management Code of Practice. The Statement sets out the proposed strategy with regard to borrowing, the investment of cash balances and the associated monitoring arrangements.

3.13.2 The proposed prudential indicators set out in the Treasury Management Strategy will be based on the proposed Capital Programme 2023-26.

## 3.14 TIMETABLE

3.14.1 Following the budget consultation process, a report will be brought to the November Cabinet which will provide a detailed update of the financial planning assumptions underpinning the current MTFS and the outcome of the budget consultation with stakeholders.

3.14.2 In the January Cabinet report, Members will be presented with updated information following the Provisional Local Government Finance Settlement (LGFS) and any impacts on the MTFS assumptions for government funding, Council Tax and Business Rates.

3.14.3 The draft timetable for the budget setting process is as follows:

| Activity | Draft Dates |
|---|---|
| MTFS and Budget Scene Setting report to Cabinet | July 2022 |
| Local Council Tax Reduction Scheme – if to be changed from 2023-24 then statutory consultation will need to begin in the late summer | LCTRS changes would require Council approval by end of January 2023 |
| Statutory Budget Consultation (businesses) | TBC |
| MTFS and Budget report to Cabinet (first version) | November 2022 |
| Fees and Charges report to Cabinet | November 2022 |
| Local Government Finance Settlement (provisional) | December 2022 |
| Local Government Finance Settlement (final) | January 2023 |
| MTFS and Budget report to Cabinet (final version) | January 2023 |
| MTFS and Budget report to Full Council and setting of Council Tax | March 2023 |
| Treasury Management Strategy report to Full Council | March 2023 |

## 3.15 BUDGET CONSULTATION AND SCRUTINY PROCESS 2022-25

3.15.1 The Council must undertake statutory budget consultation with Business Rates payers in the borough and it is also good practice to consult with Council Tax payers and a broad range of other key stakeholders. In addition, meaningful consultation must take place with service users before any changes to service provision are implemented. Furthermore, the Council's budget framework sets out the need for the Overview and Scrutiny Committee to be involved in the setting of the Council's budget.

3.15.2 The Council is intending to carry out a consultation with businesses. The consultation will aim to ask how the Council should consider its approach in light of the budgetary pressures it faces which have increased due to the impact of inflation, Brexit and the Covid-19 pandemic. It is not currently proposed to carry out a consultation with residents as their priorities have already been demonstrated through the recent election based on the administration's manifesto proposals.

3.15.3 The on-going role of the Overview and Scrutiny Committee in scrutinising business cases and undertaking targeted reviews in a number of key areas identified by them is key to maintaining the rigour of budget scrutiny of the Medium Term Financial Strategy (MTFS).

3.15.4 In addition to the scrutiny of relevant revenue savings and growth proposals the O&S Committee will undertake similar scrutiny of capital programme proposals. They will also have an overview of the medium term financial proposals being considered for approval by the board of Tower Hamlets Homes (THH), including proposals for rent setting and medium term savings. Similarly, the budget strategy for the Schools Budget which will be proposed for approval by the Cabinet, from the Schools Forum.

## 4 EQUALITIES IMPLICATIONS

4.1 The Equality Act 2010 requires the Council, in the exercise of its functions to have due regard to eliminate unlawful discrimination, harassment and victimisation, advance equality of opportunity and foster good relations between people who share a protected characteristic and those who do not.

4.2 Tower Hamlets is one of the fastest growing and most densely populated places in the UK. Our population has grown by almost 31% since 2011 to just under 332,000. It is expected to increase to 364,000 by 2028 (a further 9.6% increase). More homes are built here than almost anywhere else. The borough is expecting to accommodate a further 35,000 homes by 2028. We are a young borough - the average age is 32 and 44% of the population is between 20 and 39.

4.3 Tower Hamlets is a world borough with a proud history of diversity and equality. Over 117 languages are spoken in the borough's schools – 43% of residents were born in over 200 different countries. The mid-pandemic residents survey 2021 showed that 79% of our residents feel that people from different backgrounds get on well together.

4.4 This diversity and rapid growth mean that ensuring equality is embedded throughout Council plans, services and activities is the number one priority and at the heart of all decision making. To help meet its duty under the Equality Act the Council undertakes equality impact assessments to analyse a proposed change to assess whether it has a disproportionate impact on persons who share a protected characteristic. As part of our budget setting process an equality impact assessment checklist is carried out on all new savings and growth proposals to determine if a full equality impact assessment needs to be carried out.

4.5 Corporate Directors will ensure equality analyses are completed to inform decisions for implementation of these proposals.

4.6 In setting the 2022-23 budget, no new savings were agreed, however existing savings for 2022-23 and 2023-24 that were agreed in the 2020-23 and 2021-24 budgets will still need to be implemented or reviewed for any changes. The new growth items proposed in the 2022-23 budget represented a positive impact for residents and organisations in the borough.

## 5. OTHER STATUTORY IMPLICATIONS

5.1 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 best value is achieved.

5.2 The preparation of the MTFS takes account of the Council's obligations in relation to its Best Value duty. The budget proposals are based on securing best value within the context of continuing reductions in Council funding and service demand pressures.

5.3 The sustainable action for a greener environment implications of individual proposals in the budget are set out in the papers relating to those proposals.

5.4 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 will be reported to Cabinet as the budget process develops. The Council will maintain a range of budget provision (contingency) earmarked reserves for specific risks and general reserves for unforeseen events and risks.

5.5 The crime and disorder implications of individual proposals in the budget are set out in the papers relating to those proposals.

5.6 Any safeguarding implications of individual proposals in the budget are set out in the papers relating to those proposals.

## 6. COMMENTS OF THE CHIEF FINANCE OFFICER

6.1 As this report is primarily financial in nature the comments of the Chief Finance Officer (Section 151 Officer) have been incorporated throughout this report.

6.2 The government's Core Spending Power calculation makes assumptions about the level of growth in the Council Tax base and that authorities will increase Council Tax each year up to the referendum limit.

6.3 Not increasing the Council Tax in line with government assumptions would reduce the income available to the Council for 2023-24 and future years due to the impact on the Council's on-going tax raising base and also through the Fair Funding review where the government has indicated its preference to use a notional level of Council Tax rather than actual Council Tax levels to determine the extent of resources available to each authority. There are significant risks facing the Council's funding over the medium term due to planned Local Government funding reforms.

6.4 Due to only receiving a one-year settlement for 2022-23 from Central Government, and funding reforms signalled within the settlement, it is extremely challenging to forecast the Council's funding over the medium term. The impact of the fair funding review, business rates reset and changes pertaining to New Homes Bonus, especially in light of the government's Levelling Up agenda, will impact Tower Hamlets significantly and timing of the implementation of these reforms together with details of how funding will be redistributed, including any transitional arrangements, are unknown at this stage. Over the medium term the funding gap could be in the range of circa £10m to £30m, however the MTFS will continue to be refreshed in 2022 as more information is received on the government's intended changes to funding, to ensure a sustainable budget going forward and alignment with the refreshed Strategic Plan.

## 7. COMMENTS OF LEGAL SERVICES

7.1 The Council is required by section 151 of the Local Government Act 1972 to make arrangements for the proper administration of its financial affairs. The Council's Chief Finance Officer has established financial procedures to ensure the Council's proper financial administration. These include procedures for budgetary control of which this report forms part. It is consistent with these arrangements for Cabinet to receive information about the revenue and capital budgets from time to time and as set out in this report. It is also consistent to be continually reviewing the position on a rolling basis and setting strategic directions for the coming months.

7.2 The monitoring of budgets and financial information is also a significant contributor to meeting the Council's Best Value legal duty and therefore this report complies with that legal duty.

7.4 There are areas covered in the report where persons with a protected characteristic for the purposes of the Equality Act 2010 may be indirectly affected by the budgets as set. However, where changes in the budgetary position may result in a change to the delivery of a service, the effect on such persons will be considered separately and prior to the making of a change to that service.

**Linked Reports, Appendices and Background Documents**

**Appendices**

- Appendix 1 Draft Budget Setting Timetable
- Appendix 2A MTFS Summary
- Appendix 2B MTFS Detail by Service Area
- Appendix 3 Previously Approved Growth and Inflation
- Appendix 4 Previously Approved Savings
- Appendix 5 New Growth, Inflation and Changes to Existing Savings
- Appendix 6 Projected Movement in Reserves
- Appendix 7 Reserves Policy

**Linked Report**

- None

**Background Documents – Local Authorities (Executive Arrangements)(Access to Information)(England) Regulations 2012**

- None

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