

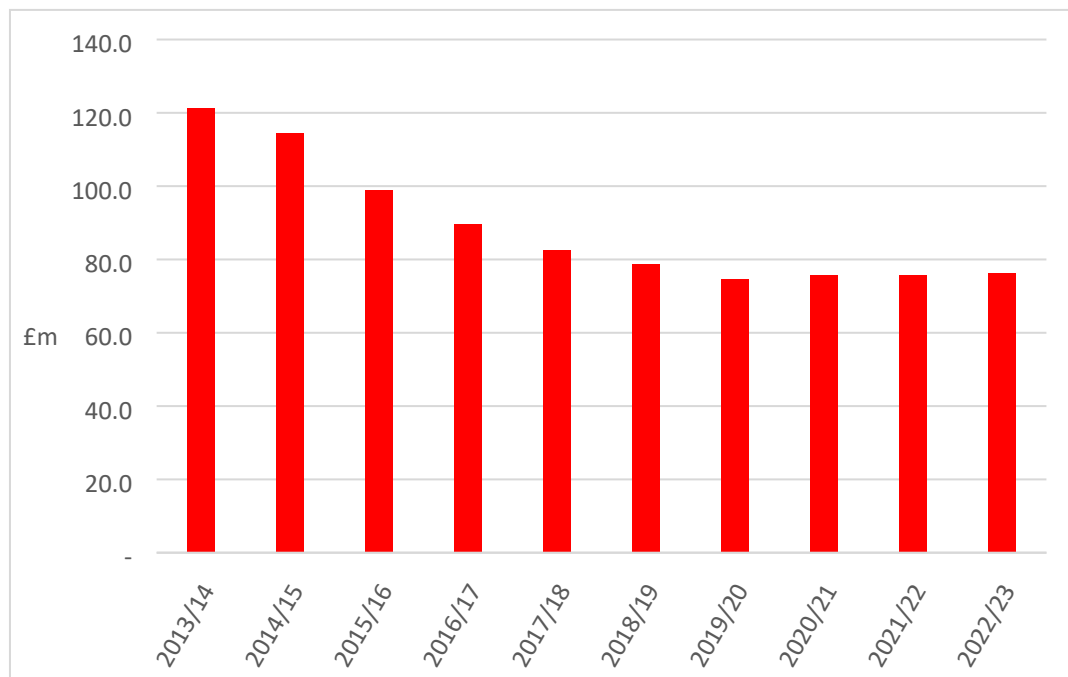
CABINET

12 July 2022

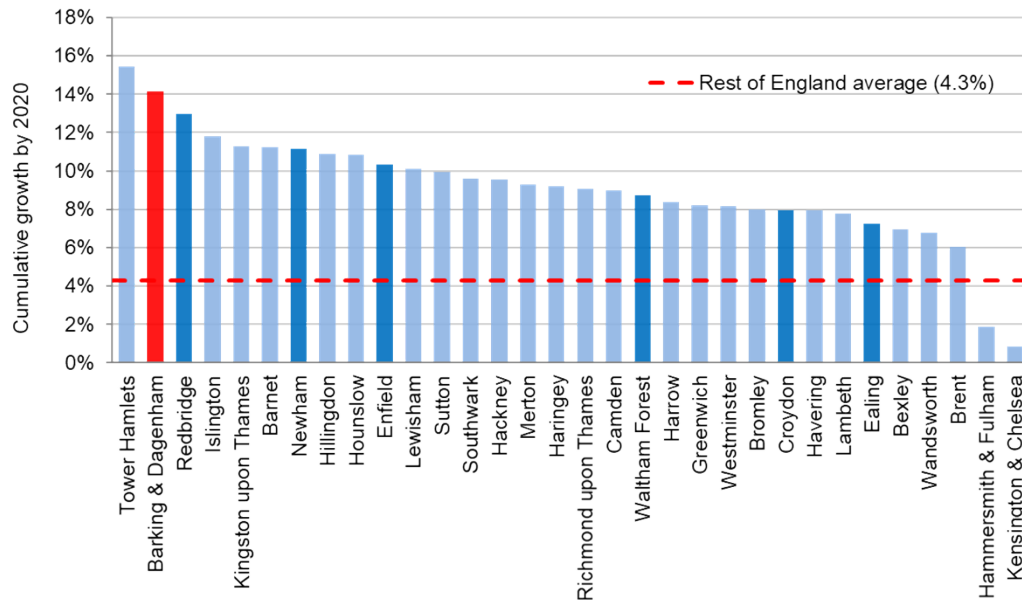
Title: Medium Term Financial Strategy and Reserves Policy 2022/23 to 2026/27	
Report of the Cabinet Member for Finance, Growth and Core Services	
Open Report	For Decision
Wards Affected: All	Key Decision: Yes
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Accountable Strategic Leadership Director: Philip Gregory, Director, Finance & Investment	
Summary <p>This report sets out a draft Medium-Term Financial Strategy (MTFS) and Reserves policy for the period 2022-23 to 2026-27 for key council (General Fund) services. It shows how the delivery of a strategy for a well run organisation goes hand in hand with organisational financial health. It has been prepared recognising the financial uncertainty arising from a period of increasing inflation following the COVID-19 pandemic and from uncertainty facing the sector in light of plans to delay fair funding reforms and 75% business rates retention until 2024-25 at the earliest, whilst taking into account anticipated demands and pressures.</p> <p>The MTFS identifies a cumulative gap of £14.8m during the MTFS period. This gap is to be closed through targets for both short-term and longer-term interventions which will require budget savings to be delivered to ensure a medium term financially balanced position. The report also sets out principles for a robust reserves policy.</p>	
Recommendation(s) <p>Cabinet is recommended to approve the Medium Term Financial Strategy and Reserves Policy 2022/23 to 2026/27 as set out in Appendices A and D to the report and the proposed approach to ensure the financial health of the Council over the medium term.</p>	
Reason(s) <p>The setting of a robust and balanced Medium Term Financial Strategy will enable the Council to provide and deliver services within its overall corporate and financial planning framework. The Medium Term Financial Strategy underpins the delivery of the Council's vision of One borough; one community; no one left behind and delivery of the priorities within available resources.</p>	

1. Introduction and Background

- 1.1. This report sets the context for the future financial position for the London Borough of Barking and Dagenham. The Medium Term Financial Strategy (MTFS) is a statement on the council's approach to the management of its financial resources to meet its Corporate Priorities. The MTFS also considers the appropriate level of reserves that the Council holds to mitigate current and longer term risks.
- 1.2. In February 2022, Assembly approved the budget for 2022-23 including an indicative forward forecast for future years.
- 1.3. The funding the Council receives from government has consistently reduced since public sector austerity was introduced in 2010-11. In 2013-14 local government were allocated a share of business rates from their area. Since 2013-14 government grants have reduced by over 40%. In 2013-14 our grant was £126m, in 2022-23 our grant is £76m.



- 1.4. Barking and Dagenham also has seen the second highest population growth in London during the same time period and almost 10% higher than the average English local authority. Our residents tend to be younger than the average in other London boroughs and many of our residents face a range of challenges and disadvantages that mean that they may need help and support from the Council at some point.



- 1.5. The combination of reducing funding and a growing population meant the Council had to do something in order to be able to continue to provide services to local residents and businesses. The Ambition 2020 programme began in 2017 and delivered a New Kind of Council whilst setting out plans to deliver almost £50m in savings and increased income. A primary focus of the programme was to maximise housing, business and economic growth within the borough.
- 1.6. The COVID-19 pandemic has had a profound and unprecedented impact on the activity and finances of the council since March 2020 and this is likely to continue throughout 2021-22 and beyond into the medium term. The pandemic has resulted in three major financial effects on the council's financial position:
 - Additional costs
 - Income loss
 - Agreed savings at risk
- 1.7. The financial scarring effects of the pandemic will continue to impact demand for services and income due to the council for many years to come. Whilst the council is not alone in facing these challenges this does not lessen the scale of the challenge and the impact on the residents and businesses within the borough.
- 1.8. The economy is also having to cope with increasing inflation resulting in a cost-of-living crisis. The impact of this is uncertain apart from a high probability that costs will increase and income sources will be unlikely to keep up. This is discussed further in section 3 of the report.
- 1.9. The financial framework was anticipated to change as a result of the Ministry of Housing, Communities and Local Government (MHCLG) Fair Funding review from 2019-20. The Government has not begun consultation on introducing these reforms during 2022 which implies that another one-year financial settlement will be provided for 2023-24 with longer term funding reforms being introduced in 2024-25 at the earliest.

- 1.10. The impact of these delays to funding reform on the council is by no means clear. However, the MTFS brings together anticipated demands and pressures and sets out how the council will ensure a balanced medium-term position.
- 1.11. Medium term financial planning must make assumptions about the future demand profile and cost pressures on expenditure and on factors that affect income sources. The MTFS represents a summary of these assumptions and their impact on the funding of the council.
- 1.12. The MTFS sets the financial envelope within which the council must fund its activities in order to set a balanced budget in each of the next 4 years. In order to begin the budget setting process for 2023-24 and beyond it is therefore prudent to revise the MTFS at the beginning of the budget setting process. Throughout the summer and autumn services plans and budgets will be produced to deliver a balanced budget for 2023-24. In addition, this process will allow the council to identify where savings may be achieved in future years and begin planning their delivery.
- 1.13. The MTFS provides assurance on the intended use and the overall level of reserves and the extent of underpinning commercial and financial planning risk.

2. Council Priorities and Strategic Framework

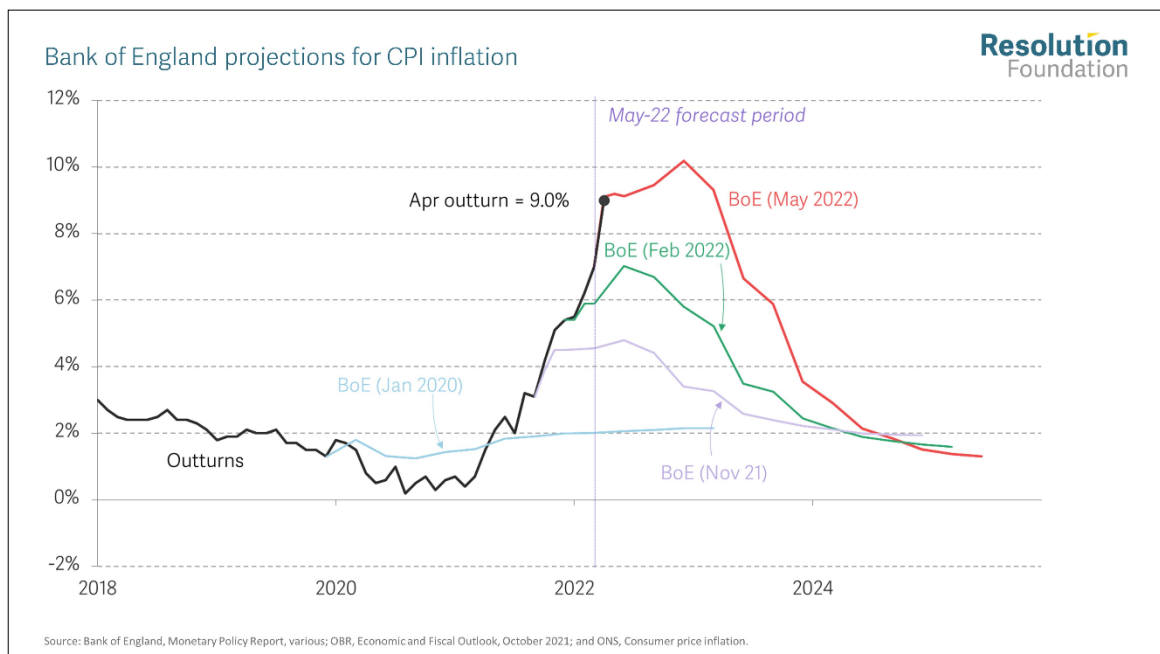
- 2.1. The MTFS is underpinned by four key strategic priorities for the council to ensure that resources are aligned with their delivery:
 - **Inclusive Growth.** All activity related to homes, jobs, place and environment will be organised into a single strategy, focused on intervening in our economy in order to improve economic outcomes for all residents.
 - **Prevention, independence and resilience.** All activity relating to people facing public service will be organised into a single strategy, focused on intervening in society in order to improve health and wellbeing outcomes for all residents, at every stage of life.
 - **Participation & engagement.** All activity related to community engagement and social infrastructure will be organised into a single strategy focused on giving every resident the power to influence local decisions, and to pursue their version of the good life.
 - **Well Run Organisation.** This is a crosscutting strategic priority, concerned with the operation of the Council's support functions and the way in which our business is operated.
- 2.2. These strategic priorities will sit alongside our continued efforts to build and embed our new kind of council and will drive all council activity in the years ahead. Critically, each has an important part to play in managing future demand on council services. The financial position set out in the MTFS is designed to reflect this position.

3. Cost of Living Crisis

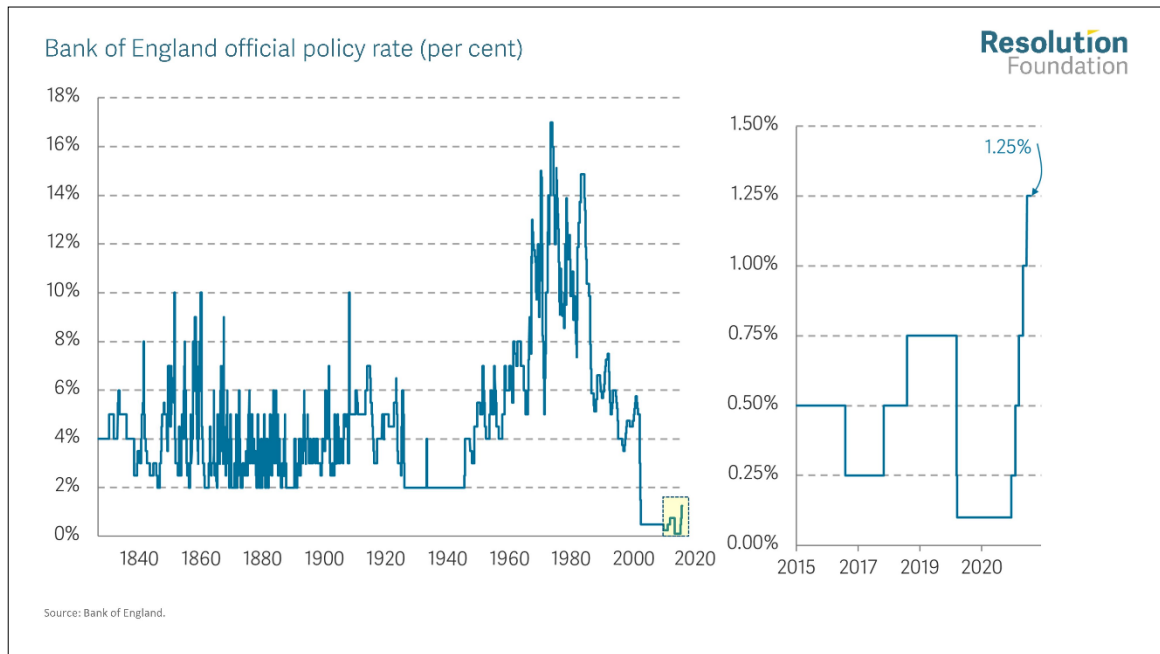
- 3.1. The cost-of-living crisis is driven by many factors that are primarily evidenced by increases in inflation (comparing current costs to how much they cost a year ago). There are a number of reasons for increasing inflation which started to increase in

2021 in large part due to increased spending on goods during the Covid crisis. As economies around the world, including in the UK, opened up after Covid restrictions eased, some businesses struggled to meet this extra demand because of difficulties in getting the materials used in their production. Recent lockdowns in China have had an impact on the supply of goods. Russia's invasion of Ukraine has led to sharp increases in the price of energy. The war in Ukraine has also caused an increase in the price of many agricultural commodities, such as grain, which are needed to produce food. There are also inflationary pressures from the UK economy including wage inflation as there are more job vacancies than there are people to fill them, which means employers are having to offer higher wages to attract job applicants.

- 3.2. Inflation has risen sharply to level not seen for many decades. On 18 May 2022, the Office for National Statistics (ONS) published data showing that twelve-month inflation in the Consumer Prices Index (CPI) was 9.0% in April (compared to 8.1% in the Euro-area and 8.6% in the US). The Bank of England forecast that CPI inflation is expected to be over 9% during the next few months and to rise to slightly above 11% in October reflecting higher projected household energy prices following an additional large increase in Ofgem price cap. Inflation is expected to fall to the 2% target by 2024 as shown below.



- 3.3. In an effort to contain inflation and return it to the Government's 2% target the Bank of England has increased interest rates in recent months to 1.25%, the highest rate for 13 years.



- 3.4. Interest rates may continue to increase over coming months with financial markets expecting rates to increase to 3%. The Bank of England are not forecasting that rates will rise to 3% although a further increase above 1.25% is expected to be announced in August.
- 3.5. The impact on the council is pronounced and creates significant financial pressure on budgets. The cost of goods and services, including energy costs, to the council are expected to increase during the current financial year. In addition the pay award for 2022-23 is likely to be greater than the 1.75% agreed for most staff in 2021-22. These cost increases will create in-year budget pressures that services will need to manage.
- 3.6. The impact on local residents and businesses will also be extremely challenging. Barking and Dagenham is the most deprived London Borough and has the highest level of unemployment in the country. The council relies on council tax and business rates income to fund services and many services have income budgets from fees and charge which may also come under pressure during 2022-23.

4. COVID-19

- 4.1. The COVID-19 pandemic occurred after many years of financial pressures for local authorities. Even without COVID-19 there were underlying overspends or pressures in a number of areas, some of which worsened during the pandemic. There has been significant financial turmoil from many different aspects of their local roles, both from the delivery of services and as a conduit for central government to support local businesses
- 4.2. The current expectation remains that there will no further Government support beyond what has been announced for previous financial years. It is expected that the demand for services will continue to emerge, particularly in social care services over the medium term.

5. Medium Term Financial Strategy Forecasts

- 5.1. The budget report to Cabinet in February 2022 set out the following financial forecasts:

Table 1: Financial position reported in February 2022

	2022-23 £m	2023-24 £m	2024-25 £m	2025-26 £m
Budget Gap (incremental)	-	6.191	10.952	9.291
Budget Gap (cumulative)	-	6.191	17.103	26.394
Council Tax Assumption	2.99%	2.99%	2.99%	2.99%

- 5.2. A review of the assumptions within the MTFS has been undertaken to inform this update, rolling forward these to 2026-27 to present the updated MTFS position. In response to increasing inflation the budget provision in 2023-24 and 2024-25 has been increased to take into account pay and price increases. In addition, the services grant from government which was expected to be provided for 2022-23 only has been included in 2023-24 and future years as the funding reforms promised from 2023-24 in place of the services grant are unlikely to materialise. Further details on assumptions within the MTFS are described in the following section of the report.
- 5.3. As shown in Table 2 the budget gap has decreased from £26.394m to £14.826m.

Table 2: Recommended changes to the MTFS

	2023-24 £m	2024-25 £m	2025-26 £m	2026-27 £m
Budget Gap (incremental)	6.191	10.952	9.291	-
Updates	0.924	(10.282)	(5.174)	-
Budget Gap (incremental)	7.115	0.670	4.117	2.924
Budget Gap (cumulative)	7.115	7.785	11.902	14.826

- 5.4. The strategy to address the funding gap is through the following routes:
- Savings proposals: those that have been identified and those that are proposed for approval in this report.
 - Delivery of the corporate plan priorities and agreed transformation programmes to deliver sustainability in the longer term.
 - Continue to identify new investment opportunities to secure financial sustainability and deliver regeneration for the borough.
- 5.5. Included within the figures in Table 2 are increased allocations for inflation and demographic growth over the MTFS period. Inflation is provided for pay and price inflation with the actual pay award for 2022-23 still outstanding. Inflation is assumed to peak during 2022 and return to 2% during 2024. Demographic growth funding is an estimate of funding that will be required as the borough population grows, recognising that the cost of providing services to these additional residents will also

grow. Services will be able to bid against these funding allocations and the final allocations for 2023-224 will be confirmed in the MTFS presented for approval by Assembly in March 2023.

Table 3: Inflation and Demographic Growth funding

	2022-23 £m	2023-24 £m	2024-25 £m	2025-26 £m	2026-27 £m
Inflation	6.228	9.267	6.665	3.941	3.999
Demographic Growth	-	4.068	4.287	4.629	4.776
Total:	6.228	13.336	10.942	8.570	8.776

- 5.6. The CFO has assessed the minimum level of general fund balances at £12m and the Council currently holds £17m.
- 5.7. The Council uses reserves to support medium term financial planning and management. This is particularly important in the current economic climate and uncertainty regarding the impact of the wider economy, continuing demand following COVID-19 and delays to local government funding reforms. The strategy of the Council, launched through Ambition 2020, was one focused on growth and investment in the borough. It is therefore necessary to hold reserves at sustainable levels to dampen the effect of short-term changes in the economy without putting at risk the longer term goal of growth.

6. Key Assumptions

- 6.1. There are a number of assumptions that underpin the updated MTFS including:
- 6.2. There is an assumption of full achievement of previously approved transformation savings of £10.35m. These savings were planned to be realised by the end of 2020-21 however these savings have been reprofiled into 2022-23 as a result of the COVID-19 pandemic. The progress of the delivery of approved savings is reported in the regular budget monitoring reports to Cabinet. Any savings that are not delivered in full will result in an overspend and an increased drawdown on reserves.
- 6.3. Settlement funding from Government will continue on the same principles that were applied in 2022-23. The Government provided a one-off services grant of £4m in 2022-23 which was to be replaced by funding reforms in 2023-24. To date the Government have not yet begun consultation on the implementation of funding reforms and so the implication is that the fair funding review and business rates reset will be introduced in 2024-25 at the earliest, if at all. It is therefore expected that the services grant will continue from 2023-24 providing additional funding of over £5m per year.
- 6.4. Indicative council tax increases of 2.99% have been included. This may include a proportion of Adult Social Care Precept although the Government are yet to publish guidelines on council tax referendum limits. Growth in the council tax base has been estimated by using data on expected new homes being occupied over the MTFS period. A prudent deduction has been made to account for properties that may be delayed or where council tax will not be payable in full, e.g., recipient of

CTS. On this basis the growth in council tax base has increased from 1.5% to 3% per year. This results in additional council tax income as shown in the table below.

	2023-24	2024-25	2025-26	2026-27
Council tax base – 1.5% growth	52,860	53,653	54,458	55,274
Council tax base – 3.0% growth	53,641	55,250	56,908	58,615
Increase in council tax base	781	1,598	2,450	3,341
Band D council tax estimate	£1,403.78	£1,473.56	£1,517.62	£1,563.00
Increase in council tax income	£1.117m	£2.355m	£3.718m	£5.222m

- 6.5. New Homes Bonus funding will continue to be allocated until the Fair Funding review is implemented on a single year basis. Legacy payments from previous years will continue to unwind.
- 6.6. Growth in budgets has been included where this has previously been agreed by Cabinet.

7. Budget Risks

- 7.1. There are a number of risks that continue to influence the MTFs including the following:
- 7.2. **Recovery from COVID19:** The impact of COVID-19 on the demand for statutory services and the finances of the Council will continue to evolve throughout 2022-23. Costs and income assumptions will need to be monitored with care throughout 2022-23 to ensure that emerging risks are brought to the attention of Members in a timely way.
- 7.3. **Brexit:** The impact on Local Government upon leaving the EU may continue to have significant impacts on funding from Government, especially as the economic, social and financial implications of Brexit and subsequent trade deals become clearer. There will be a continued assessment of the impact to the council as a result of the referendum vote to leave the EU which could include impacts on interest rates, migration, employment and business.
- 7.4. **Capacity to deliver approved savings:** If agreed savings are not achieved this will result in overspends and budget shortfalls in future years. Regular monitoring and reporting takes place, however, non-achievement of savings will require compensating reductions and management action to find compensating cost reductions where savings are no longer possible.
- 7.5. **Government funding:** The Government intends to change current funding mechanisms to reflect an increased emphasis on need and to reset the current business rates retention system. These proposals are expected to be delayed by at least another year which carries a high degree of uncertainty into the quantum of Government funding in 2022-23 and beyond. In the light of the extreme uncertainty surrounding Government funding the MTFP has included forecast income in 2022-23 based on current assumptions.

- **Budget and Spending Review:** A Spending Review from the Government is expected in the autumn. It is unclear whether this will be a single year or multi-year Spending Review and therefore whether local government will receive a single year or multi-year Settlement. Our current assumption is that there will be a one-year settlement whilst the Government continues to monitor the economic effect of inflation on the wider economy.
- **Levelling Up:** Levelling up funding is currently being delivered through grant funding which must be bid for competitively for specific projects. It is unclear what impact the levelling up agenda will have on funding other than to state the fair funding review and business rates reset could be tools to deliver the missions of levelling up.
- The **Fair Funding Review** of local government is likely to shift resources away from London. The design of new funding formula is predicated on moving to a more dynamic, realistic method of allocating funding that is able to respond to demographic changes. On this basis and considering the demographic changes within Barking and Dagenham, this approach may prove beneficial to us. We expect the new funding formula to be used to allocate funding from 2024-25 at the earliest.
- The **Business Rates Retention** scheme is also being redesigned and is expected to be introduced from 2024-25 at the earliest. It is anticipated that the implementation of 100% business rates retention will be accompanied by additional responsibilities and therefore an increase in the costs borne by Local Government. The details of these responsibilities are to be confirmed.
- The **New Homes Bonus** funding for 2023-24 is expected to be allocated for one year only and will not result in legacy payments in future years. It is expected that the New Homes Bonus funding will be wrapped up within the Fair Funding Review in following years. It is unclear how the Government will incentivise local authorities to deliver additional housing within the new funding regime.

7.6. **Achievement of Council Priorities:** The strategic framework requires appropriate oversight and governance to ensure it is delivered through effective programme management. Where performance indicators are not on target, corrective action will be required.

7.7. **Commercial Risks** arise from undertaking investments and from action taken by the Council's subsidiaries. These risks can be mitigated through effective due diligence on new commercial investments and continued robust appraisals of subsidiary business plans and forecast returns. The Shareholder Panel monitors the performance of the subsidiaries against their respective business plans and holds the Board of each company to account for the delivery of the strategic and financial objectives. Where planned financial returns are delayed or profitability is reduced there will be a direct cost to the Council to mitigate such losses.

7.8. **Demand Pressures** arise from changes within the population and economic activity within the Borough. Assumptions on future demand for services have been included in the MTFS. Exceptional demands, particularly as a result of increasing inflation, that emerge will result in spending control within departments or corporate budgets.

7.9. **Pension Fund** risks include changing economic conditions and investment returns less than assumptions in the Pension Fund's investment strategy increases the risk

of a deterioration in the Pension Fund's funding position and as a consequence there is a risk of an increase in the employer's contribution.

- 7.10. **Legislative changes** or the imposition of new responsibilities upon the council without adequate funding remains a risk.
- 7.11. Impact of variations to forecast **interest rates**, both in terms of investment returns and also on assumptions made on borrowing costs. Interest rate risks are managed through effective treasury management and the use of fixed rate loans where appropriate.

8. Review of Reserves

- 8.1. Reserves are used to manage risks and are either usable or unusable. Unusable reserves arise from statutory accounting transactions and cannot be used to fund revenue or capital expenditure. This report only considers the Council's usable reserves. The Council's Reserves Policy is included in **Appendix C**.
- 8.2. A review of reserves has been carried out as at 31 March 2021 and balances based on the draft final accounts are summarised in **Appendix D**.
- 8.3. General fund balances are set aside to provide an emergency fund for exceptional circumstances. This fund is reviewed regularly and assessed as a minimum of £12m. Currently, the Council has some £17m in this reserve.
- 8.4. The forward forecast of reserves is maintained by the CFO using assumptions on certain investment decisions and no additional budget pressures emerging during the course of the current financial year. A further review of reserves will take place later in the year.
- 8.5. The aim of the Medium Term Financial Strategy is to set out an affordable financial plan that provides for sustainable levels of spending, not dependent upon the use of one-off reserves, whilst providing for a prudent level of reserves for contingencies.

9. Approach to Budget Setting for 2023-24

- 9.1. The Medium Term Financial Strategy identifies a savings requirement of £14.8m by 2026-27. Proposals to meet this savings requirement will be presented to Cabinet in December alongside a public consultation for all proposals members are happy to proceed with as part of the Budget consultation process. The proposals, along with consultation results will be presented again to Cabinet in advance of Assembly in February.

10. Financial Implications

Implications completed by: Philip Gregory, Director Finance & Investment (S151 Officer).

- 10.1. The detailed financial implications have been covered throughout the report. Members are asked to note the revised MTFS position as set out in section 5 of this report.

11. Legal Implications

Implications completed by: Dr Paul Feild, Senior Governance Solicitor

- 11.1. A local authority is required under the Local Government Finance Act 1992 to produce a 'balanced budget'. It must look and plan further and during any financial year, there is an ongoing responsibility to monitor spending and ensure the finances continue to be sound. This does mean as a legal requirement there must be frequent reviews of spending and obligation trends so that timely intervention can be made ensuring the annual budgeting targets are met. Furthermore, the Council is subject to the Best Value duty under the Local Government Act 1999 to secure continuous improvement in an efficient, economic and effective way.
- 11.2. Section 25(1)(a) and (b) of the Local Government Act 2003 requires its Chief Finance Officer (Section 151 Officer) to report on the robustness of the estimates made for the purpose of calculating Council Tax, but more particular to the purposes of this report the adequacy of reserves hence the need for a Reserves Policy. When considering what level of general reserve to hold applicable legislation includes s.31A, 42 and 43 of the Local Government and Finance Act 1992.
- 11.3. If during the Strategy period there are reductions or changes in service provision as a result of changes in the financial position the local authority is free to vary its policy and consequent service provision but at the same time must have regard to public law considerations in making any decision lawfully as any decision eventually taken is also subject to judicial review. Members would also wish in any event to ensure adherence as part of good governance. Specific legal advice may be required on the detailed implementation of any agreed savings options. Relevant legal considerations are identified below.
- 11.4. Whenever there are proposals for the curtailment or discontinuance of a service or services, there will be a need for appropriate consultation. In some cases, this will be prescribed by statute, or by common / case law. For example, if savings proposals will affect staffing then it will require consultation with unions and staff. In addition to that Members will need to be satisfied that Equality Impact Assessments have been carried out before the proposals are decided by Cabinet and proper consideration of human rights. If at any point resort to constricting expenditure is required, it is important that due regard is given to statutory duties and responsibilities. The Council must have regard to:
 - any existing contractual obligations covering current service provision. Such contractual obligations where they exist must be fulfilled or varied with agreement of current providers;
 - any legitimate expectations that persons already receiving a service (due to be cut) may have to either continue to receive the service or to be consulted directly before the service is withdrawn;
 - any rights which statute may have conferred on individuals and as a result of which the Council may be bound to continue its provision. This could be where an assessment has been carried out for example for special educational needs statement of special educational needs in the education context);
 - the impact on different groups affected by any changes to service provision as informed by relevant equality impact assessments;

- to any responses from stakeholders to consultation undertaken.

12. Corporate Policy and Equality Impact

- 12.1. The Equality Act 2010 requires a public authority, in the exercise of its functions, to have due regard to the need to eliminate discrimination and to advance equality of opportunity between persons who do and those who do not share a relevant protected characteristic. As well as complying with legislation, assessing the equality implications can help to design services that are customer focussed, in turn leading to improved service delivery and customer satisfaction.
- 12.2. The Council's Equality and Diversity strategy commits the Council to ensuring fair and open service delivery, making best use of data and insight and reflecting the needs of the service users. Equality Impact Assessments allow for a structured, evidence based and consistent approach to considering the equality implications of proposals and should be considered at the early stages of planning.
- 12.3. There are no new savings proposals that put forward and EIAs have also been carried out for all existing saving to ensure the Council properly considers any impact of the proposal. The Council's transformation programme aims to redesign services to make them more person-centred and focussing on improving outcomes for residents. Therefore, in most cases the proposals have either a positive or neutral impact. However, where a negative impact has been identified, the Council will ensure appropriate mitigations are considered and relevant affected groups are consulted.

Public Background Papers Used in the Preparation of the Report: None

List of appendices:

- Appendix A – Medium Term Financial Strategy 2022/23 to 2026/27
- Appendix B – Budget Growth and Savings
- Appendix C – Reserves Policy 2022/23 to 2026/27
- Appendix D – Reserve Balances as at 31 March 2022