

# Crawley Borough Council

## Report to Overview & Scrutiny Commission 29 October 2018

### Report to Cabinet 31 October 2018

## Budget Strategy 2019/20 – 2023/24

Report of the Head of Corporate Finance, **FIN/417**

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### 1. Purpose

- 1.1 The 2019/2020 General Fund and Housing Revenue Account Budgets and the updated capital programme will be determined by the Full Council in February 2019. This report sets out the projected financial position for 2019/20 to 2023/24 for the General Fund and the underlying assumptions.

The report also sets the policy framework for the budget process, recognising that there are a range of options for capital investment, income generation, savings and Council Tax levels; none of which can be considered in isolation. The overall objective is to work towards a balanced General Fund budget over a three year period.

- 1.2 A separate report on the Housing Revenue Account's capital investment programme will be considered by the Budget Advisory Group ahead of the Budget report to Cabinet and Full Council in February 2019.

### 2. Recommendations

#### 2.1 To the Overview & Scrutiny Commission

**That the Commission consider the report and decide what comments, if any, it wishes to submit to the Cabinet.**

#### 2.2 To the Cabinet:

**The Cabinet is asked to recommend to Full Council the approval of the Budget Strategy 2019/20 to 2023/24 and to:**

- (a) **Note, for the purpose of projections, the current budget deficit of £225,000 for 2019/20, on the basis of a Council tax increase of £4.95 on a Band D in 2019/20.**
- (b) **Work towards balancing this over a three year period, including putting back into reserves when the Budget is in surplus.**
- (c) **To transfer £1m from the Business rates equalisation reserve to the General Fund reserve; and in addition any in year and future surplus are to be**

**transferred to the General Fund reserve in order to fund the short term additional costs due to the investment in the New Town Hall build as outlined in section 7.6 below.**

- (d) Instruct Corporate Management Team to take action to address the long term budget gap and to identify policy options for consideration by Cabinet Members and the Budget Advisory Group, which will include areas where additional resources need to be redirected.**
- (e) Note that items for the Capital Programme are driven by the need for the upkeep of council assets and environmental obligations and schemes will also be considered that are spend to save or spend to earn.**
- (f) Note that the Budget is aligned to the Council's Corporate Priorities.**

### **3. Reasons for the Recommendations**

- 3.1 To set a Strategy for savings and income generation and working towards a balanced budget over three years. Including putting back into reserves when the budget is in surplus.
- 3.2 To determine the criteria for capital programme bids.
- 3.3 To agree the level of reserves in section 7.6 in order to support funding the shortfall budget shortfall as a result of the investment in the New Town Hall project.

### **4. Background**

- 4.1 The local government finance system has become increasingly complex. The difficulty of predicting what factors such as interest rates, Government funding and other costs will be in two to five years' time is further complicated by uncertainty regarding the financial impact of the European Union Referendum and the Government's Fair Funding Review.
- 4.2 On 17 December 2015 the Department of Communities and Local Government (DCLG) announced that councils would be able to achieve greater certainty and confidence from a DCLG 4 years Budget Settlement (this covers 1 April 2016 to 31 March 2020). The offer covered all councils that receive Revenue Support Grant (RSG), from 2016/17 to 2019/20. The proposals show that Crawley will receive just £59,107 in RSG in 2019/20. This is compared to £4.9m received in 2013/14.
- 4.3 The 2019/20 General Fund and Housing Revenue Account Budgets and the revised capital programme will be set by the Full Council in February 2019. This will be informed by the recommendations of the Budget Advisory Group and will take into account the efficiencies, increased income and savings achieved through a refreshed transformation programme and budget challenge process led by the Corporate Management Team. Work to address this has started and will continue over the Autumn.
- 4.4 Many of the underlying financial assumptions in this report apply equally to the Housing Revenue Account as to the General Fund (for example inflation and employee related costs). However, the financial position of the Housing Revenue Account (HRA) is heavily influenced by the financing regime introduced in April 2012.

Under this regime the Council has taken on debt of £260.325m and determined a repayment profile which gives it the capacity to spend capital sums to achieve some of its objectives for housing. This includes a comprehensive stock investment programme and the building of new Council homes.

However this was complicated by the Government's announcement in the July 2015 Budget that rents are to be reduced by 1% per annum for 4 years from 2016/17. This reduced the Council's ability to invest in the provision of new housing.

The Council has been selected to bid for additional borrowing to build more housing. A bid has been made to the Ministry of Housing, Communities & Local Government (MHCLG) in order to build up to an additional 231 affordable homes. These are made up of 183 affordable rent units and 58 shared ownership units. The outcome of the bids will be known later this year and will be reported to Cabinet and Full Council. Subsequently to this an announcement was made at the Conservative Party conference that the debt cap will be removed. Details of this will follow in the Budget on 29<sup>th</sup> October 2018.

## 5. Key Assumptions

- 5.1 This report provides details of budget projections for a five year period, 2019/2020 to 2023/2024. There are a number of key assumptions affecting the projections. A summary table is shown in paragraph 5.11.

On 24 July 2018, the (MHCLG) issued a technical consultation paper on the 2019-20 settlement. In that paper there are no proposed changes to the limits on council tax increases in 2019-20 (a maximum of £5 on a Band D property), although they are still subject to confirmation in the provisional settlement which will be announced around Christmas 2018.

### 5.2 External support

The Local Government Finance four year settlement gives the Council's Revenue Support Grant and is shown in the table below

	2016/17	2017/18	2018/19	2019/20
Provisional RSG	£1.76m	£1.04m	£0.57m	£0.06m
Percentage reduction	-32.35%	-41.64%	-44.54%	-89.72%

The 2019/20 figures show that the Council will receive £59,107 in Revenue Support Grant and no grant thereafter.

### 5.3 Retained Business Rates

Although the Council will collect in excess of £119 million in business rates, the amount it retains is much smaller. One of the main reasons for this is that the Government retains 50% of the rates collected and West Sussex County Council retains 10%. The second main reason is that the Council also has to pay a significant **tariff** to the Government.

There are further complications in that the Council's retained share can be added to by a safety net payment, or suffer a further levy. These are applied if the Council's retained share is more than 7.5% below a Government set figure (safety net) or above it (a levy of 50%).

The Council is in a levy position, so as a result for every additional £1 that it collects above its funding target, it only keeps 20p.

An annual increase in line with RPI in 2019/20 and then CPI thereafter in business rates is included in the Budget Strategy. This will be reviewed regularly to allow for any growth and provision for appeals.

Any in year variations from this budget will be transferred to/from the business rates equalisation reserve. When the reserve exceeds £5m the surplus is transferred to the general fund or capital programme reserve. Section 7.6 below looks to reduce this reserve to £4m which will be sufficient to manage in year variations.

As part of the MHCLG consultation a further round of 75% business rates retention pilots 2019 to 2020 has been announced. The terms offered for 2019-20 are not as good as those available in 2018-19 as pilots will only retain 75% of any gain compared to 100. West Sussex Authorities are submitting a bid to become a pilot in this round; the outcome will be known late Autumn.

#### **5.4 Pay Award**

Local Government pay is negotiated nationally and the Council has no direct influence on the settlement. The agreed increase is 2%, however there are changes to the grading structure with spinal columns amalgamated and new ones created together with higher than 2% increases for many of the lower spinal column points. The impact of these results is an overall increase of 2.802%; the cost of the pay award is estimated to be £497,000.

The table in 5.11 shows future assumptions.

#### **5.5 Investment Interest**

5.5.1 The Council has traditionally relied heavily on investment interest to support the revenue budget. However, interest rates remain low and the level of interest received has reduced over recent years.

5.5.2 The Bank of England increased the base rate to 0.75% in August 2018 – the highest level since March 2009. The Monetary Policy Committee (MPC) has indicated that future base rate increases will be gradual and would rise to a much lower equilibrium rate than before the financial crisis. Our treasury advisors are forecasting that the MPC will not increase the base rate again before the Brexit deadline in March 2019. They feel that the MPC is more likely to wait until August 2019 before the next increase, to be followed by further increases in May and November 2020 to reach 1.5%. However, the uncertainty around the Brexit agreement means that this forecast is highly uncertain.

5.5.3 An average investment rate of 1.00% has been assumed for 2019/20, increasing to 1.25% in 2020/21 and 1.50% in 2021/22. Interest rate projections will be kept under constant review during the year.

5.5.4 Expenditure on the capital programme results in reduced investment income as there are fewer resources available for investment, and future investment balances will be much lower once development of the new Town Hall begins. However, delays in the capital programme will result in higher balances available than anticipated for investment.

#### **5.6 Pensions**

5.6.1 The actuarial revaluation of the pension fund managed by West Sussex County Council has resulted in a 0.5% increase in contributions in 2019/20.

#### **5.7 General Inflation**

In recent years many budgets have been frozen or reduced which has compensated for those budgets that have increased by more than the base assumption (for example energy and fuel). The Budget Strategy assumes that contract costs linked to inflation indices will increase by 3.7% in 2019/20, reducing to 3.2% by 2022/23. These assumptions will be updated over the coming months. No allowance has been made for inflation on other general running expenses.

## 5.8 **New Homes Bonus**

- 5.8.1 The Government introduced the New Homes Bonus (NHB) to give local authorities additional money for each new residential property created in the area. Local authorities would receive a sum equivalent to the average national Council Tax for a property in that band for each of the following six years. For example, at that time an additional band D property will result in £1,590 being paid for six successive years.
- 5.8.2 There is an additional payment of £350 for each year if the property falls into the definition of affordable housing. This additional element is paid a year in arrears. In two tier areas the District or Borough Council receives 80% of the bonus and the County Council 20%.
- 5.8.3 The Government made changes to the way that the NHB operated when the number of years of legacy payments was reduced from 6 to 5 years in 2017/18, and then down to 4 years in 2018/19. In addition a national baseline (or deadweight) was introduced in 2017/18. It was set at 0.4% in 2017/18 and remained at this level in 2018/19. The stated purpose of both these changes was to “sharpen the incentive” for local authorities. In reality, the national baseline allowed the Government to manage the cost of the NHB scheme. By applying these changes the Government was able to reduce the cost of the scheme from £1.6bn in 2016/17 to £900m in 2019/20.

In the [technical consultation](#) paper, the Government reminds authorities that the scheme already allows it to increase in the national baseline to manage the cost of the scheme. The upward trend in house-building suggests that the national baseline (deadweight) will be increased from 0.4% in 2019/20.

The New Homes Bonus for 2019/20 is projected to be £1.531m and is estimated to reduce to zero by 2023/2024. The reason for this reduction is that in the consultation the MHCLG state that it is the Government’s intention to explore how to incentivise housing growth most effectively, for example by using the Housing Delivery Test results to reward delivery or incentivising plans that meet or exceed local housing need. These assumptions will be refined once the outcome of the consultation is known.

## 5.9 **Fees and Charges**

An average increase in income budgets of CPI or 2%, whichever is the highest is assumed for 2019/20 onwards.

## 5.10 **Fair Funding review**

The Government are reviewing the way in which local authorities in England are funded in their ‘Fair Funding Review’. Central government funding for local authorities is based on an assessment of its relative needs and resources. The overarching methodology that determines how much funding each authority receives each year was introduced over ten years ago and has not been updated since funding baselines were set at the start of the 50 per cent business rates retention scheme in 2013/14.

The methodology is very complex and involves 15 relative need formulas and several tailored distributions for services previously supported by specific grants. These formulas involve over 120 indicators of ‘need’, reflecting factors previously identified as driving the costs of service delivery. It is widely agreed across the sector that the formulae are overly complex, lack transparency and, as they have not been updated for a long time, are now out of date.

The government is therefore undertaking the Fair Funding Review to update the needs formula and set new funding baselines for the start of the new 75 per cent business rates retention scheme, from April 2020.

The outcome of this review will not be known until late in 2019. It is therefore very difficult to project forward and setting the 2020/21 budget will result in transferring either to or from reserves.

#### 5.11 Summary of assumptions

	<u>19/20</u>	<u>20/21</u>	<u>21/22</u>	<u>22/23</u>	<u>23/24</u>
Business rate income*	+3.7%	+2.2%	+2.1%	+2.0%	+2.0%
New Homes Bonus	£63k	-£307k	-£483k	-£421k	-£320k
Pay award	2.802%	2.0%	2.0%	2.0%	2.0%
Av. interest rate	1.00%	1.25%	1.50%	1.65%	1.75%
Running costs	0%	0%	0%	0%	0%
Contracts (RPI)	3.7%	3.4%	3.3%	3.2%	3.2%
Customer receipts	2.5%	2.2%	2.1%	2.0%	2.0%
Tax base increase (percentage of new properties for Council tax)	1.5%	1.5%	1.5%	1.5%	1.0%
Council Tax increase (for estimating purposes)	2.5%	2.4%	2.3%	2.3%	2.3%

\*Business rates equalisation reserve will be used to absorb any fluctuations.

The tax base increase assumes the number of Band D properties in Crawley has increased due to the current building programme including Crawley Homes new builds.

## 6. Budget Projections 2019/20 to 2023/24 (excluding the costs of the New Town Hall)

6.1 The table below summarises the budget projections based on the assumptions above.

	2019/20 £'000s	2020/21 £'000s	2021/22 £'000s	2022/23 £'000s	2023/24 £'000s
Base budget	14,909	15,290	15,683	16,208	16,674
Investment interest	(1,086)	(1,141)	(1,278)	(1,454)	(1,453)
Net budget	13,823	14,149	14,405	14,754	15,221
Funded by:					
Council Tax	7,188	7,449	7,704	7,999	8,265
New Homes Bonus	1,531	1,224	740	320	0
Retained Business Rates	4,056	4,366	4,462	4,555	4,647
Section 31 Grant*	764	780	798	814	831
Assumed reduction for Fair Funding		(700)	(1,000)	(1,250)	(1,500)
Revenue support Grant	59	0	0	0	0
<b>Budget Gap / (Surplus)</b>	<b>225</b>	<b>1,030</b>	<b>1,701</b>	<b>2,316</b>	<b>2,978</b>

\* Section 31 Grant is payable by the Government when they give business rate discounts for small businesses

Costs associated with the New Town Hall have been excluded at this stage as final contracts have yet to be signed (with the exception of sums currently in the capital programme).

6.2 There is a projected budgeted gap in 2019/20 of £225,000; increasing to £1,701,000 by 2021/22. At this stage there is an assumed reduction in funding as a result of the Fair Funding Review of £700,000 in 2020/21 increasing annually. Once the outcome of the review is known these assumptions will be amended.

The Table below summarises the movements in the Gap

	2019/20	2020/21	2021/22
	£000's	£000's	£000's
Inflation	468	824	1,196
Interest	-238	-294	-431
Retendered contracts	-645	-635	-625
CMT restructure	-123	-123	-123
Business rates income	340	14	-99
Increased Council tax income	-258	-519	-773
Heat Pump at Tilgate Park	-38	-38	-38
Planning pre-applications fees	-30	-30	-30
Reduced External audit fees	-15	-15	-15
Annual IT licence costs (revenue implications of capital programme)	64	64	64
Reduced recycling credit income from WSCC*	203	203	203
New Homes Bonus	-63	244	727
Fair Funding – estimate	0	700	1,000
Reduced Revenue Support Grant	516	575	575
Increased Employers pension contributions	73	73	73
Other – various	-29	-13	-3
<b>Total</b>	<b>225</b>	<b>1,030</b>	<b>1,701</b>

\*West Sussex County Council have notified all West Sussex Districts that it is 'encouraging improved recycling performance'. In a letter from the Director of Energy, Waste and Environment, councils are told that West Sussex County Council are in a difficult financial position with £74m budget deficit over the next three years and that the current cost sharing mechanism is very generous compared to most other partnership agreements or the default rate. As a result the County Council are changing their methodology which will save them £1.038m and as a result the payment to Crawley Borough Council will be £203,135 based on current tonnes per annum recycle.

The aim is to have a balanced budget over a three year period. In the event of an in year surplus this will be transferred to reserves.

6.3 The assumptions above include a provision for a Council Tax increase close to £5 (£4.95 in 2019/20) per annum on a Band D property. This is less than 10p per week. The aim is to work to keep council tax low without compromising local services.

#### 6.4 **Budget pressures**

Any additional growth items approved as part of future years budgets will increase the budget gap over the long term. There are however areas where there may be the need for investment in services. These include

- Data and information management and IT staffing levels
- Town Centre cleaning

## **7. General Fund Reserves**

- 7.1 The Council achieved a surplus General Fund in 2017/18 of £0.923m, which was transferred to the capital programme reserve.
- 7.2 There are two purposes for holding reserves. The first is to have sufficient funds to be able to maintain services, both in the short and medium term. The second is to earmark funds for specific purposes. There should be plans to spend earmarked reserves, even if the amount and timing of that spending is uncertain.
- 7.3 The level of reserves should be regularly reviewed. This is particularly true in the current situation. Local government has had reduced financial resources from the Government and it is clear that this is going to continue for several years. Other Government changes (for example the localisation of Council Tax Benefit and of Business Rates) have transferred significant risks to local authorities.
- 7.4 For both the Housing Revenue Account and the General Fund, the Council needs sufficient funds to be able to sustain services. In the case of the Housing Revenue Account the reserves are sufficient and no changes are proposed.
- 7.5 The 2016/17 Budget Strategy set the General Fund reserve at £4m and a separate business rates equalisation reserve for £5m. Any reserves available in excess of these sums are transferred to the Capital programme reserve.
- 7.6 Due to the short term impact of the expenditure on the New Town hall it is proposed that any surplus in the current financial year (Projected at £309,000 at Quarter 1) and in the financial year 2019/20 are transferred to the General Fund reserve. In addition, that £1m is transferred from the Business rates equalisation reserve to the General Fund reserve. This will still allow for volatility within the Business rates system to allow for any in year fluctuations between budgets and income.
- 7.7 This will provide sufficient sums within the General Fund reserve to fund budget shortfalls during the new build programme and at the same time allow the reserve not to get below £2.5m.
- 7.8 Further details of the impact of the New Town hall will be included in the Quarterly budget monitoring reports to Cabinet.

## **8. Capital Funding**

- 8.1 Future bids for capital should be based on expenditure required to maintain the Council's assets, for environmental obligations such as flood prevention and for disabled facilities grants. In addition bids will be for spend to save projects or spend to earn investment income. Schemes will be presented to the Budget Advisory Group later in the year for prioritisation. Once the New Town hall project has commenced future capital commitments will result in borrowing. The Treasury Management Strategy which will be reported to Cabinet and Full Council in February 2019 will address any borrowing requirements. In addition a Capital Strategy report will go to the same meetings.
- 8.2 Any other specific bids will be presented directly to later meetings of the Cabinet.



## **9. Housing Revenue Account**

- 9.1 Council on 22 February 2012 (FIN/257) approved the payment of £260.325m to the Department for Communities and Local Government as part of the Government's abolition of the previous housing subsidy regime. The money was borrowed via a series of loans from the Public Works Loan Board. The repayment dates vary between 2022/2023 and 2037/2038.
- 9.2 The net effect of these changes was that the HRA had budgeted for significant surplus over the coming years. This was to enable the Council to make capital investments that will help it achieve its corporate housing objectives. Investments already approved include the provision of housing at Breezehurst Drive, Brunel Place and Forge Wood. Changes to Right to Buy discounts and the announcement in the July 2015 budget that rents will decrease by 1% per annum for 4 years from 2016/17, resulted in fewer resources available to meet all aspirations.
- 9.3 The HRA 30 year plan is constantly being updated, and is reported to the affordable housing group. This takes both revenue and capital budget projections and shows resources available for future investment in housing.
- 9.4 There was an announcement at the Conservative Party conference that the debt cap will be removed. This would allow an increase in borrowing in order to build more housing. Further details will be available in the Budget on 29<sup>th</sup> October and will be reported to future Cabinet meetings and Full Council.

## **10. Budget Process**

- 10.1 The Budget Advisory Group will be meeting over the coming months to assess the policy implications of savings measures, future growth bids and business cases put forward to support proposals for capital investment including Crawley Homes. The report of the Chair of the Budget Advisory Group will be considered by the Cabinet in the New Year.
- 10.2 The Budget and Council Tax report will be considered by the Cabinet on 6 February 2019. The 2019/20 Budget will be set by Council on 27 February 2019.
- 10.3 Where budgetary proposals identify the need for the reduction of, or closure or discontinuance of a service, appropriate consultation will need to be carried out. The Council will also have to have due regard to the public sector equality duty under section 149 of the Equality Act 2010 in making their decisions. The equalities impact will be addressed on proposals as they are developed.

## **11. Background Papers**

[2018/19 Budget and Council Tax FIN/434](#)  
[Budget Strategy 2018/19 - 2022/23 FIN/417](#)  
[Treasury Management Strategy 2018/19 FIN/433](#)  
[Financial Outturn 2017/2018 FIN/443](#)  
[Treasury Management Outturn 2017/18 FIN/442](#)

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