



**Budget and Policy Framework 2019 - 2023**  
**12 February 2019**

**Report of the Interim Head of Financial Services**

| PURPOSE OF REPORT   |                 |                  |  |          |
|---|-----------------|------------------|--|----------|
| This report sets out the latest position in respect of the budget and policy framework including Cabinet's proposed revenue budget for 2019/20 and Capital Programme for 2019/20 to 2022/23. The report also sets out the Treasury Management Framework for Cabinet adoption and provides an update on the revision of the Medium Term Financial Strategy |                 |                  |  |          |
| Key Decision  | X               | Non-Key Decision |  | Referral |
| Date of notice of forthcoming Key Decision  | 14 January 2019 |                  |  |          |
| This report is public.  |                 |                  |  |          |

**RECOMMENDATIONS OF COUNCILLOR WHITEHEAD:**

- 1) That Cabinet recommend the following for approval to Budget Council:
  - The 2019/20 General Fund Net Revenue Budget and resulting Council Tax Requirement excluding parish precepts (Appendix A) and supporting budget proposals (Appendix B).
  - The S151 Officer's statement on the adequacy of reserves and advice that the minimum level of balances be increased to £2m, subject to annual review.
  - the resulting position on provisions and reserves (Appendix C)
  - The updated five year Capital Programme (Appendix D) covering financial years 2018/19 to 2022/23.
- 2) That the Finance Portfolio Holder be given delegated authority to agree the Treasury Management Framework, as updated for Cabinet's final budget proposals, for referral on to Council.
- 3) That the Finance Portfolio Holder be given delegated authority to agree the revision of the Medium Term Financial Strategy, as updated for Cabinet's final budget proposals, for referral on to Council.

## 1 INTRODUCTION

- 1.1 Under the Constitution, Cabinet has responsibility for developing corporate planning processes and a balanced revenue budget and capital programme for Council's consideration.
- 1.2 The Council meeting on 30 January considered Cabinet's proposed revenue budget for 2019/20 and approved a City Council Tax increase of 2.99% together with a year on year target of 2.99%, for the purposes of financial planning, over the period of the Medium Term Financial Strategy.
- 1.3 Cabinet has also considered capital programme bids for 2019/20 to 2022/23 and this report provides a proposed capital programme for consideration and recommendation to Budget Council. The Treasury Management Strategy takes account of the proposed capital programme.
- 1.4 The report seeks delegated authority for the Finance Portfolio Holder to agree the Treasury Management Framework, subject to any changes made to capital programme proposals before it is referred to Budget Council.
- 1.5 A draft update of the Medium Term Financial Strategy has also been completed for Cabinet's consideration and referral on to Budget Council.

## 2 REVENUE BUDGET 2019/20

- 2.1 A general fund revenue budget for 2019/20 is included at **Appendix A** with more detailed budget proposals in **Appendix B**. The proposed budget is balanced, in line with statutory requirements, and takes account of the final local government finance settlement which was approved by Parliament on 5 February 2019.
- 2.2 Cabinet is now required to finalise its full budget proposals and make recommendations to Budget Council.
- 2.3 The proposed revenue budget was agreed by Cabinet at its meeting on 15 January and this was subject to the final local government settlement and calculations of annual estimates for collection fund surpluses or deficits in respect of council tax and business rates which are considered below.

### **Final Local Government Settlement**

- 2.4 The final Local Government Settlement was published on 29 January 2019 and approved by Parliament on 5 February 2019. There were no changes to the Lancaster City Council allocations announced in the provisional settlement. Parliament also agreed council tax threshold principles which for districts provide for a maximum increase in precept of 3% or £5, whichever is higher.

### **Council Tax**

- 2.5 Legislation requires that separate estimates be made for any Collection Fund surpluses or deficits on the Collection Fund relating to the council tax and business rates.
- 2.6 For council tax, it is confirmed that the Collection Fund is expected to be broadly balanced and therefore there is no surplus or deficit to distribute.

- 2.7 As there were no changes to council tax referendum thresholds, the Council Tax increase of 2.99% agreed by Council on 30 January means that the City element of Council Tax for a band D property will be £226.95, subject to rounding adjustments, representing an annual increase of £6.59.

### **Business Rates**

- 2.8 The Council is required to submit its annual business rates return to the Government by the end of January in which it estimates business rates income for 2019/20 and the estimated deficit / surplus as at the end of 2018/19.
- 2.9 The estimated surplus for 2018/19 is £739k as shown in the table below.

|   | 2018/19<br>£000 |
|---|-----------------|
| Actual surplus brought forward (from collection fund statement)   | (9,330)         |
| Transfer to other precepting authorities in respect of last year forecast surplus (arising from calculations done a year ago) | 7,429           |
| Forecast Business Rates Income for 2018/19  | (61,437)        |
| Rate Retention Scheme Charges for 2018/19   | 62,599          |
| Estimated Surplus for 2018/19 as at 31 January 2019   | (739)           |
| City Council Share of the surplus at 40%  | (296)           |

- 2.10 Business rates continues to be an area of uncertainty in respect of predicting income for two primary reasons set out below:
- The potential for a shutdown at Heysham Nuclear Power Station continues to be a risk which the Council has to monitor, as such an event would significantly reduce retention from business rates. The Council has, since the start of the localised rates scheme, budgeted at 'worse case' whereas actual retention income has exceeded the budget. This additional income has been added to a Business Rates Reserve which provides increased financial resilience in case of a future shutdown at the power station.
  - The Council receives a 'disregard' for renewable energy hereditaments which means that 100% of the business rates for these properties is retained by the authority. It is estimated that in 2019/20, this will be worth £906k to Lancaster City Council. Whilst it is evident that this 100% disregard will continue into 2019/20, there is a risk that the Government will discontinue this advantageous arrangement at some point in the future.

### **3. PROVISIONS, RESERVES AND BALANCES**

- 3.1 Under current legislation the Section 151 Officer is required to give explicit advice to Council on the minimum level of reserves and balances.

#### **Provisions**

- 3.2 The bad debt and insurance provisions have been reviewed and are considered adequate at this time.

## Balances – General Fund Balance

3.3 The Section 151 Officer's latest advice on the adequacy of balances is based on the following observations:

- The General Fund Balance at 31/03/18 was £5,069m.
- Latest revenue budget monitoring forecasts a very modest overspend of £13k in 2018/19. This would reduce the General Fund Balance to £5,056m.
- The Council's MTFS suggests a budget gap in 2020/21 onwards in excess of £2m. If this is not closed then balances will be required to make the difference.
- There is a significant level of uncertainty with respect to Council funding particularly in respect of both retained rates and New Homes Bonus and there is a possibility that the Council's funding will be reduced as a result of the Fair Funding Review.
- Business rates retention volatility remains a risk to the Council but this is now managed via the Business Rates Reserve considered in the next section and therefore should not impact on the General Fund balance.
- There is continuing uncertainty with respect to Brexit and how this might impact, directly or indirectly, Council finances.
- The MTFS provides forecasts on funding and on net expenditure and sensitives associated with these forecasts. Moreover, the Capital Strategy documents collectively provide assurance with respect to the affordability, sustainability and prudence of capital expenditure.

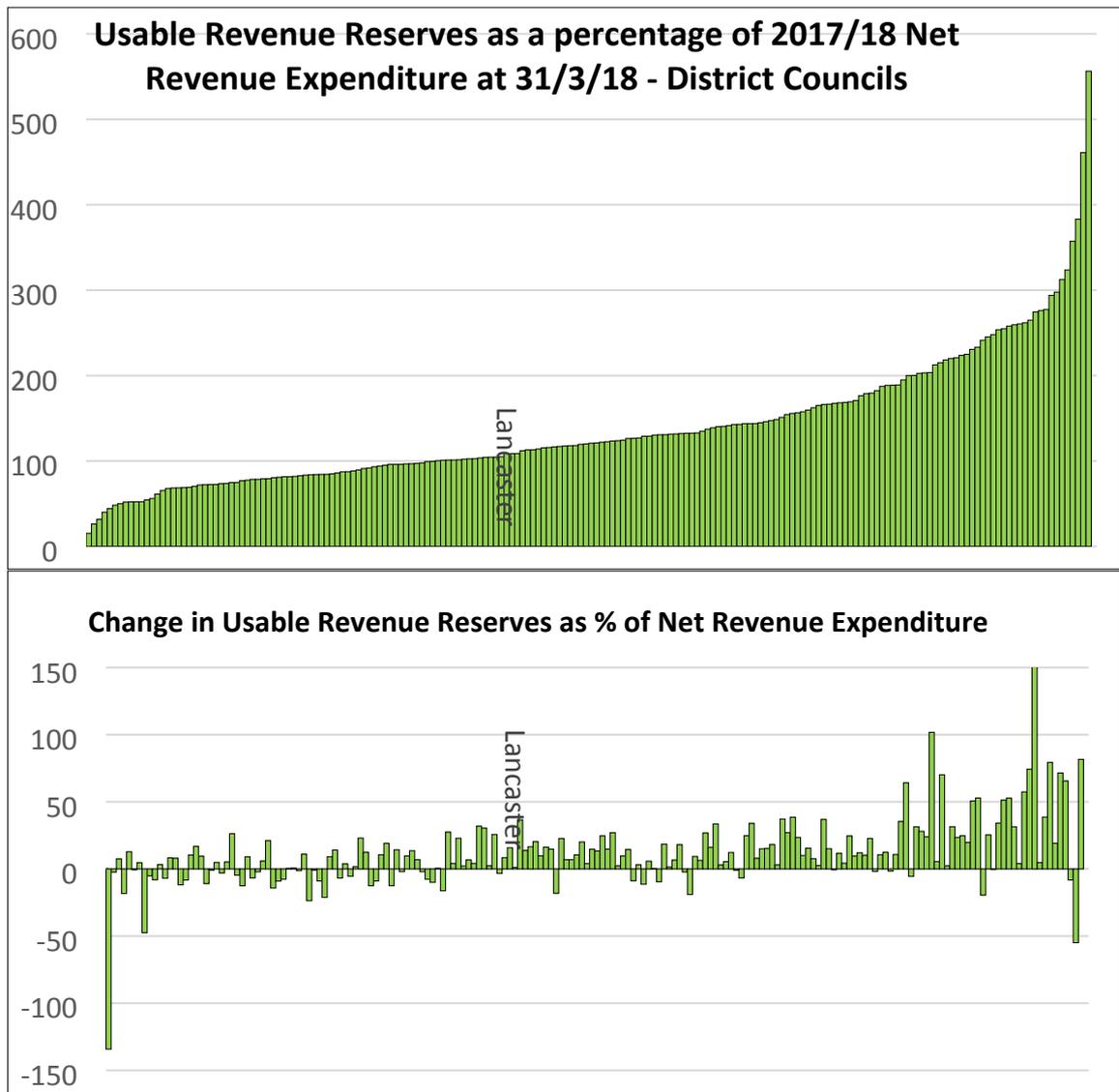
3.4 In calculating the minimum level of General Fund balance, an assessment of the risks that give rise to unanticipated expenditure or loss of income has been made and these are shown in the table below. The analysis shows that, in the unlikely event of a 'perfect storm' of risks happening all within the next year, there are sufficient balances to meet all these risks in the short term which would give the Council time to adapt in the longer term.

| Risk  | Symptom of risk                                | Balance required<br>£000 |
|---|--|--------------------------|
| Increased demand for services                             | 3% increase in net revenue expenditure         | 500                      |
| Recession results in reduced fees and charges income      | 10% reduction in major fees and charges income | 657                      |
| Recession results in reduced council tax collection rates | 3% reduction in collection rate                | 282                      |
| New Homes Bonus scrapped                                  | Significant reduction in funding income        | 1,242                    |
| Next year's budget savings not achieved                   | Significant overspend                          | 1,083                    |
| Natural disaster such as flood                            | Additional unanticipated expenditure           | 500                      |
| Uncertainty with respect to Brexit                        | Additional unanticipated expenditure           | 500                      |
| Aggregate overspend if all above risks were to happen     |  | 4,764                    |
| General Fund Balance as at 31/03/18                       |  | 5,069                    |

- 3.5 Whilst it is highly unlikely that all the above events would occur at the same time, it is nevertheless a more uncertain time with respect to funding and expenditure with the results of the Fair Funding review expected to be incorporated into the finance settlement from 2020/21 onwards. **Taking this additional risk into account, the Section 151 Officer's advice is that the minimum level of balances held in the General Fund should be set at £2m, an increase of £0.5m.**
- 3.6 The minimum level of balances will be kept under review as part of the MTFS and reported to Cabinet on a regular basis.

### Earmarked Reserves

- 3.7 Forecast earmarked reserve levels are set out in **Appendix C**. Earmarked reserves are forecast to increase significantly in 2018/19 mainly due to business rate growth. This improves the Council's financial resilience and when taken with the General Fund balance provides a level of usable revenue reserves which is equivalent to about a year's worth of net revenue expenditure. The graph below compares Lancaster's usable revenue reserve levels with all other district councils which should give some assurance with respect to adequacy of reserves.



### **Business Rates Reserve**

- 3.8 This reserve was set up to manage fluctuations in business rates income and the risks attributable to business rates appeals and the potential shutdown of Heysham Power Station. However, in six years these risks have not materialised and the Council has been able to accrue the rewards from good levels of business rates growth in the Lancaster district. Going forward, the risks persist but as part of the MTFS, an assessment of the exposure to those risks has been undertaken and it is calculated that there are surplus funds in the business rates reserve over and above those which are required to protect business rates income over the medium term. As the surplus funds are effectively attributable to economic growth it seems appropriate that consideration be given to redirecting their use towards corporate priority initiatives.

### **Budget Support Reserve**

- 3.9 The budget support reserve's purpose should be extended to include any upfront costs which are attributable to work undertaken in respect of the Funding the Future strategy. Any such bid to the reserve should be accompanied by a business case showing the need for intervention and outcomes and impact arising from the use of the reserve.

### **Reorganisation Reserve**

- 3.10 All three Directorates created under the recent reorganisation will commence structural reviews during 2019/20. There may be a significant call upon this reserve for costs relating to redundancy and pension strain but any call on the reserve should be accompanied by a payback calculation which compares the upfront cost with ongoing savings.
- 3.11 The MTFS incorporates a Reserves Strategy which covers specific plans for the above reserves. It is recommended that Cabinet delegate the finalisation of the Reserves Strategy to the Finance Portfolio Holder, as part of the MTFS refresh, prior to referral to Budget Council.

## **4 GENERAL FUND CAPITAL PROGRAMME**

- 4.1 The Capital Programme for 2019/20 to 2022/23 is set out in **Appendix D** and is summarised in the table below.

|                                | <b>18/19</b> | <b>19/20</b> | <b>20/21</b> | <b>21/22</b> | <b>22/23</b> | <b>Total</b>  |
|--------------------------------|--------------|--------------|--------------|--------------|--------------|---------------|
|                                | <b>£m</b>    | <b>£m</b>    | <b>£m</b>    | <b>£m</b>    | <b>£m</b>    | <b>£m</b>     |
| Disabled Facilities Grants     | 2.65         | 2.36         | 1.61         | 1.61         | 1.61         | <b>9.84</b>   |
| Vehicles & Plant               | 0.81         | 1.46         | 2.30         | 0.52         | 0.79         | <b>5.87</b>   |
| Sea & River Defence Works      | 2.43         | 0.45         | 0.43         | -            | -            | <b>3.30</b>   |
| Council Properties             | 0.48         | 2.72         | -            | -            | -            | <b>3.20</b>   |
| Econ. Dev. & Regeneration      | 0.33         | 1.29         | -            | -            | -            | <b>1.62</b>   |
| Parks, Sport & Recreation      | 0.21         | 0.12         | 1.00         |              |              | <b>1.33</b>   |
| ICT Infrastructure & Equip.    | 0.29         | 0.23         | 0.33         | 0.10         | 0.34         | <b>1.29</b>   |
| Solar Energy                   | -            | 0.36         | 0.32         | -            | -            | <b>0.68</b>   |
| S106 Funded Schemes            | 0.15         | 0.14         | -            | -            | -            | <b>0.29</b>   |
| Car Parks & CCTV               | 0.10         | 0.07         | -            | -            | -            | <b>0.17</b>   |
| <b>Total</b>                   | <b>7.45</b>  | <b>9.20</b>  | <b>5.99</b>  | <b>2.23</b>  | <b>2.73</b>  | <b>27.59</b>  |
| <b>Funded by</b>               |              |              |              |              |              |               |
| Capital Receipts               | -0.20        | 0.00         | 0.00         | 0.00         | 0.00         | <b>-0.20</b>  |
| Capital Grants & Contributions | -5.22        | -2.42        | -1.61        | -1.61        | -1.61        | <b>-12.47</b> |
| Capital Reserves               | -0.86        | -0.86        | -0.12        | -0.06        | 0.00         | <b>-1.90</b>  |
| Revenue                        | -0.01        | -            | -            | -            | -            | <b>-0.01</b>  |
| Unsupported Borrowing          | -1.16        | -5.92        | -4.26        | -0.56        | -1.12        | <b>-13.02</b> |
| <b>Total</b>                   | <b>-7.45</b> | <b>-9.20</b> | <b>-5.99</b> | <b>-2.23</b> | <b>-2.73</b> | <b>-27.59</b> |

4.2 In setting the capital programme the Council must have regard to affordability and the Treasury Management Strategy sets out the impact of the Council's Capital Programme on its borrowing to ensure that all borrowing is affordable, prudent and sustainable.

## 5. TREASURY MANAGEMENT STRATEGY

5.1 The Code of Practice on Treasury Management ("the Code") requires that a strategy outlining the expected treasury activity for the forthcoming 3 years be adopted, but that it be reviewed at least annually. It needs to reflect treasury policy and cover various forecasts and activities, in order to integrate the Council's spending and income plans with decisions about investing and borrowing.

5.2 To give context, and for information, the Quarter 3 monitoring report for the current year is included as part of the Corporate Financial Monitoring report elsewhere on this agenda.

5.3 Over the years, the regulatory and economic environment has changed significantly and this has led the sector to consider more innovative types of investment activity. Reflecting this, Members will be aware that changes have been made regarding the capital and treasury management framework.

5.4 The main objective of these changes was to respond to the major expansion of local authority investment activity over the last few years into the purchase of non-financial investments, particularly property. The updated framework distinguishes between treasury management activities and investment in non-financial investments.

- 5.5 Treasury management activities represent the placement of residual cash held in the bank resulting from the authority's day to day activities in relation to S12 Local Government Act investment powers. The Treasury Management Strategy, therefore deals principally with investments and borrowing.
- 5.6 Non-treasury investments would include commercial investments whereby the objective is primarily to generate capital or revenue resources. The resources generated would then help facilitate the delivery of council services.
- 5.7 The Prudential Code 2017 also introduced a new requirement to produce an annual capital strategy. This is an over-arching corporate document which deals with the key areas of strategic context, corporate priorities, capital investment ambition, available resources, affordability, capacity to deliver, risk appetite, risk management and determining an appropriate split between non-financial and treasury management investments in the context of ensuring the long term financial sustainability of the authority. It sets the context for the Treasury Management and Investment Strategies. The Capital Strategy is included elsewhere on this agenda.

### **Treasury Management Framework**

- 5.8 The proposed Strategy for 2019/20 to 2022/23 is set out at **Appendix G** for Cabinet's consideration. The document contains the necessary details to comply with both the Code and Government investment guidance. Responsibilities for treasury management are set out at **Appendix E** and the policy statement is presented at **Appendix F**.
- 5.9 Key elements and assumptions feeding into the proposals are outlined below. These take account of Cabinet's existing budget proposals as far as possible at this stage. Should there be any changes to the budget, then the treasury framework would need to be updated accordingly before being referred on to Budget Council. For these reasons, delegated arrangements are being sought for finalising the framework.

### **Borrowing Aspects of the Strategy**

- 5.10 Based on the draft budget, for now the physical borrowing position of the Council is projected to remain fairly constant over the next three years, allowing for scheduled repayments. It is also projected that the HRA capital programme will not require any additional borrowing.

### **Investment Aspects of the Strategy**

- 5.11 Overall, the strategy put forward follows on from 2018/19 in that it is based on the Council having a comparatively low risk appetite with focus on high quality deposits. The 2019/20 strategy continues to use the same investment criteria as approved by Members in 2018/19.
- 5.12 The proposed investment aspects of the strategy for treasury activities continues to provide for investing with other local authorities given that these, in effect, are as secure as investing with the Government but they offer greater returns, and from an Officer perspective, it makes sense to keep the benefits of such temporary cash investing/borrowing wholly within the local authority family.

## **6. MEDIUM TERM FINANCIAL STRATEGY**

6.1 The proposals set out in this report will be incorporated into the refresh of the Medium Term Financial Strategy (MTFS) so that this can be presented to Budget Council. The MTFS covers the following areas:

- Using the balanced revenue budget for 2019/20 as a base, a forecast of funding and net revenue expenditure for the next four years has been undertaken to understand the future funding gap.
- Initial high level plans for bridging the gap are explored which include actions arising from the Funding the Future strategy, reorganisations and proactive asset management.
- A new Capital Strategy; an overarching document which sets the policy framework for the development, management and monitoring of capital investment. It incorporates the Property Investment Strategy, Asset Management Plan and Treasury Management Framework. The Strategy which sets out revised management and governance arrangements which will be key as ambitious economic development, property investment and proactive asset management projects come forward for consideration.
- A MTFS Action Plan to be agreed by Cabinet and monitored by Budget and Performance Panel in order to ensure that the authority focuses on the budget gap in a timely and effective manner

6.2 Cabinet have received a briefing on the MTFS and following on from decisions in this paper it is recommended that Cabinet delegate the authority to finalise the document to the Finance Portfolio Holder prior to consideration at Budget Council.

## **7. CONSULTATION**

### **Revenue Budget Proposals**

7.1 Cabinet's initial budget proposals were presented to the January meetings of Budget and Performance Panel and Council.

### **Treasury Management Framework**

7.2 Officers have liaised with Link Asset Services, the Council's Treasury Advisors, in developing the proposed framework. The framework will be considered by Budget and Performance Panel at its meeting on 19 February.

## **8 OPTIONS AND OPTIONS ANALYSIS**

### **Revenue Budget**

8.1 Cabinet may adjust its revenue budget proposals, as long as the overall budget for 2019/20 balances and fits with the proposed council tax level.

### **Capital Programme**

8.2 Cabinet may adjust its capital investment and financing proposals to reflect spending commitments and priorities but in deciding its final proposals should have regard to the prudential code requirements that all capital expenditure should be prudent, affordable and sustainable.

## **Treasury Management Framework**

- 8.3 Cabinet may put forward alternative proposals or amendments to the proposed Strategy in **Appendix G**, but these would have to be considered in light of legislative, professional and economic factors, and importantly, any alternative views regarding the Council's risk appetite. As such no further options analysis is available at this time.
- 8.4 Furthermore, the Strategy must fit with other aspects of Cabinet's budget proposals, such as investment interest estimates and underlying prudential borrowing assumptions, feeding into Prudential and Treasury Management Indicators. There are no options available regarding other components of the overall framework, as covered in **Appendices E and F**.

## **9 OFFICER PREFERRED OPTION AND JUSTIFICATION**

### **Revenue Budget, Capital Programme and Reserves Position**

- 9.1 Proposals to be put forward by Cabinet should fit with any external constraints and the budgetary framework already approved. The recommendations as set out meet these requirements; the detailed supporting budget proposals are then a matter for Members.

### **Treasury Management Strategy**

- 9.2 To approve the framework as attached, allowing for any amendments being made under delegated authority prior to referral to Council. This is based on the Council continuing to have a comparatively low risk appetite regarding the security and liquidity of investments particularly, but recognising that some flexibility should help improve returns, whilst still effectively mitigating risk. It is stressed that in terms of treasury activity, there is no risk free approach. It is felt, however, that the measures set out above provide a fit for purpose framework within which to work, pending any update during the course of next year.
- 9.3 If Cabinet or Budget Council changes its Capital Programme from that which is proposed in this report then this would require a change in the prudential indicators which are part of the Treasury Management Strategy. Delegation to the Finance Portfolio Holder is therefore requested in order to ensure that Cabinet's final capital programme proposals are reflected in the Treasury Management Strategy.

### **RELATIONSHIP TO POLICY FRAMEWORK**

The budget should represent, in financial terms, what the Council is seeking to achieve through its Policy Framework

The proposed Treasury Management framework forms part of the Council's budget and policy framework, and fits into the Medium Term Financial Strategy.

## **CONCLUSION OF IMPACT ASSESSMENT**

(including Diversity, Human Rights, Community Safety, Sustainability etc)

None directly arising in terms of the corporate nature of this report – any implications would be as a result of specific decisions on budget proposals affecting service delivery.

## **FINANCIAL IMPLICATIONS**

The Strategy is in support of achieving the borrowing cost and investment interest estimates included in the budget.

## **OTHER RESOURCE IMPLICATIONS**

None directly arising.

## **SECTION 151 OFFICER'S COMMENTS**

The Local Government Act 2003 placed explicit requirements on the s151 Officer to report on the robustness of the estimates included in the budget and on the adequacy of the Council's reserves. A summary of the s151 Officer's advice to date is provided below for information, but it should be noted that some of this is provisional until Cabinet's final budget proposals are confirmed. At Budget Council, Members will be recommended to note formally the advice of the s151 Officer.

### **Provisions, Reserves and Balances**

- Specific earmarked reserves and provisions are satisfactory at the levels currently proposed.
- Unallocated balances of £2.0m for General Fund are reasonable levels to safeguard the Council's overall financial position, given other measures and safeguards proposed, and taking a medium to longer term view. This level has been increased by £0.5m compared with last year to reflect uncertainty with respect to government funding after the Fair Funding review.

### **Robustness of Estimates**

A variety of exercises have been undertaken to establish a robust budget for the forthcoming year. These include:

- producing a base budget, taking account of service commitments, pay and price increases and expected demand / activity levels as appropriate, and the consideration of key assumptions and risks.
- reviewing the Council's services and activities, making provision for expected changes;
- reviewing the Council's MTFS, together with other corporate monitoring information produced during the year;
- undertaking a review of the Council's borrowing needs to support capital investment, in line with the Prudential Code.

These measures ensure that as far as is practical, the estimates and assumptions underpinning the base budget are robust.

## Affordability of Spending Plans

In addition, the s151 Officer is responsible for ensuring that when setting and revising Prudential Indicators, including borrowing limits, all matters to be taken into account are reported to Council for consideration as part of the Treasury Management Framework.

In considering affordability, the fundamental objective is to ensure that the Council's capital investment remains within sustainable limits, having particular regard to the impact on council tax (for General Fund). Affordability is ultimately determined by judgements on what is 'acceptable' - this will be influenced by public, political and national influences.

The factors that have been (and should be) taken into account in considering capital investment plans include the following.

- availability of capital resources, including capital grants, capital receipts, etc
- existing commitments and planned service / priority changes
- options appraisal arrangements and robust business cases for chosen options
- revenue consequences of any proposed capital schemes, including interest and debt repayment costs of any borrowing
- future years' revenue budget projections, and the scope to meet borrowing costs
- the likely level of government support for revenue generally
- the extent to which other liabilities can be avoided, through investment decisions.

In considering and balancing these factors, the capital proposals to date are based on a modest net increase in "prudential borrowing" or CFR over the period to 2022/23. The bulk of this relates to service infrastructure (notably vehicle renewals, property and ICT) and completion of Invest to Save initiatives (Salt Ayre). Appropriate appraisal/procurement arrangements are in place to help ensure robustness of the plans and to support sound decision-making.

## LEGAL IMPLICATIONS

Legal Services have been consulted and have no further comments.

## MONITORING OFFICER'S COMMENTS

The Deputy Monitoring Officer has been consulted and has no further comments.

## BACKGROUND PAPERS

None.

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## Appendices

|            |  |
|------------|--|
| Appendix A | General Fund Revenue Budget Projections 2019/20 to 2022/23 |
| Appendix B | Summary of Cabinet's Budget Proposals 2019/20 to 2022/23   |
| Appendix C | Reserves Statement (Including Unallocated Balances)        |
| Appendix D | General Fund Capital Programme                             |
| Appendix E | Responsibilities for Treasury Management                   |
| Appendix F | Treasury Management Policy Statement                       |
| Appendix G | Treasury Management Strategy for 2019/20 to 2022/23        |