Somerset West and Taunton Council

Scrutiny Committee – 7 July 2021

Financial Strategy 2021/22 to 2022/23

This matter is the responsibility of Executive Councillor Ross Henley

Report Author: Paul Fitzgerald, Assistant Director – Finance (S151 Officer)

1 Executive Summary / Purpose of the Report

1.1 The Financial Strategy is presented for approval by the Executive. This sets out the approach and plans for ensuring the Council continues to operate in a financially sustainable way and allocates its resources in accordance with agreed priorities. The Strategy if agreed with underpin the ongoing management of the current year 2021/22 budget as well as the approach to developing the 2022/23 budget for approval by Council in February 2022.

1.2 The Council's services, costs and income last financial year were significantly impacted by the COVID pandemic, with major uncertainty and a frequently changing financial position. In such a dynamic and uncertain environment, financial forecasting and planning is extremely difficult, and the approach during the year necessarily adapted as the year progressed. The refresh of the financial strategy last year focused very much on managing the financial impact of COVID as well as supporting intervention and economic recovery.

1.3 Financial planning uncertainty remains, and this is reflected within the 2021/22 budget and reserves plan. The ongoing impact on services, costs and income will be carefully monitored during this year to assess reliability of current year baselines and budget forecast assumptions.

1.4 A further factor considered in the Financial Strategy is the prospect of a move to a new (one or two) unitary authority structure within Somerset from April 2023. The Secretary of State is expected to decide on the preferred option in the summer. This added uncertainty leads to a shorter-term focus in budget planning within this Strategy, with future corporate and service priorities, structural design, and related financial plans beyond 2022/23 likely to be undertaken through shadow/transitional governance arrangements.

1.5 The other major uncertainty reflected in the Strategy is future funding arrangements for local government. The previous Spending Review in 2020 only covered one year, and it is uncertain at this stage whether the 2021 Spending Review will cover a longer period, and how future funding of local government will be affected by the ongoing impact of COVID in the economy and local demand for services. Changes in funding mechanisms, such as the fair funding review and redesign of business rates retention and new homes bonus are also 'known unknowns' at this stage.

1.6 Given the level of uncertainty and likely structural change, this Strategy and updated

MTFP focus on 2021/22 and 2022/23 with an indicative forecast for 2023/24 based on continuation of existing district services.

2 Recommendations

2.1 The Executive approves the Financial Strategy 2021/21 to 2022/23.

2.2 The Executive recommends Council approves the revisions to the Budget and planned reserve transfers in 2021/22 as set out in Table 1 and Appendix A.

3 Risk Assessment

3.1 The Financial Strategy considers a wide range of financial risks, and these are explained within the detail of this report.

4 Links to Corporate Strategy

4.1 The financial strategy seeks to set out how the Council will respond to its financial challenges and how its resources are allocated to meet the Council's strategic priorities and objectives. Directly within theme 4 of the strategy, the aim is to maintain a financially self-sufficient Council which has expanded its commercial activity and generated more income to support service provision. This continues to be reflected in this Financial Strategy.

5 Financial Strategy Overview and 2022/23 Budget Approach

Context

5.1 The Financial Strategy sets out the approach to providing resources required to deliver the Council's priorities, and to ensuring services are financially sustainable. Financial planning continues to reflect the scale of risk and uncertainty both in terms of service related costs and income, and regarding projected funding through government grants, taxation and commercial investment. The Council has concentrated on stabilising and improving services following a period of change including the formation of the Council in 2019. Despite ongoing funding risk and uncertainty, the financial strategy has sought to minimise adverse impact on services through detailed work on aligning budgets with organisational design and accountabilities, pursuing commercial investment to generate additional income, and judicious use of reserves.

5.2 The last financial year 2020/21 was particularly challenging as the Council responded to the COVID pandemic, which resulted in rapid changes to service priorities. It also created added volatility and uncertainty in respect of costs and income. Overall, the Council incurred significant additional costs and income reductions, which were managed through a combination of emergency grant funding and use of the Council's own reserves. This has been reported through budget monitoring with more detail provided in the separate 2020/21 Financial Outturn report.

5.3 The Government has provided additional COVID-related funding in 2021/22 and a continuation of the compensation grant scheme mitigating approximately 70% of reductions in sales, fees and charges income for the first three months of the year. Despite the planned easing of COVID restrictions, there continues to be risk and uncertainty in 2021/22 and there could still be a long lasting impact of COVID both economically and in terms of service demand. Officers will continue to closely monitor service costs, income and funding to ensure risks are managed effectively.

5.4 Core funding from Government continues to be uncertain, and although general grant represents a small proportion of overall funding, total grant funding beyond 2021/22 is yet to be clarified. The last two Spending Reviews were for one year only with the next Spending Review due in 2021, which should set out the Government's priorities for local government. In addition, changes are expected in settlement funding, business rates retention and New Homes Bonus schemes, making it difficult to accurately predict future funding.

5.5 Hinkley Point B nuclear power station has a significant influence on the Council's funding, with the station providing almost 20% of the business rates tax base. Its rateable value (£20.72m) was reduced by some 90% for the majority of 2020/21 as the reactors were shut down for maintenance, however it has returned to its full value in early April 2021. A contingency is included in the 2021/22 budget to underwrite potential volatility during the year. EDF has announced that Hinkley B will be decommissioning by no later than July 2022, and the 2022/23 Business Rates Retention budget has been reduced to the Safety Net in anticipation, reducing annual funding by approximately £2m per year.

5.6 The Council has made good progress in building its commercial property investment portfolio during 2020/21 and is expected to complete total planned investment in 2021. This investment is on track to achieve its income target, providing essential funding for local services as other funding continues to decline.

5.7 It is well reported that the national economy experienced unprecedented decline during 2021 due to COVID and is showing signs of recovery in 2021 as restrictions are eased. Despite the economic challenges, our strategic treasury investment funds continue to deliver investment income broadly in line budget expectations although interest on short term cash funds is extremely low / zero. In addition, bank base rates and cost of borrowing remain low with short term borrowing costs very low too. This is projected to remain the case for some time, enabling projected borrowing costs to be reduced within the budget and MTFP.

5.8 The financial planning context is also now affected by the expected implementation of a unitary model of local government in Somerset, with a Secretary of State decision expected in early summer this year regarding the preferred structure; and the transitional governance arrangements that will be required prior to a new structure being implemented in April 2023. Two business cases for change have been submitted to Government – “One Somerset” and “Stronger Somerset”. This prospective change brings further uncertainty in the short term, with the service and financial priorities as well as detailed service design work to be undertaken in future through transitional arrangements. This context makes it difficult to plan for any significant change in service priorities and resources in the interim. It also signals the likelihood of significant implementation costs, albeit with longer term savings potential, which means it is prudent to plan SWTC’s use of resources and reserves with this in mind.

5.9 Somerset West and Taunton currently benefits from ongoing prudent financial management with adequate reserves and a measured balance sheet, which supports the proposed strategy set out below.

Approach

5.10 Given the context set out above the Council’s leadership proposes the following updated strategy for 2021/22 and 2022/23.

- Core spending and income assumptions will continue to be updated to reflect up to date information. A further review will be undertaken during the summer, including a reassessment of base budget requirements taking into account the 2020/21 outturn and budget monitoring in Q1/Q2 of 2021/22.
- Continuing to challenge and manage spending on services with the potential to deliver reductions in net service costs, for example through improvement, efficiency and modernisation projects and robust procurement and contract management arrangements.
- Protect funding for services in the short term to maintain service delivery and capacity to support structural change to local government in Somerset.
- Optimising treasury costs through continued access to shorter term, low cost borrowing for the next 1-2 years.
- Reinvesting investment surpluses and treasury savings to fund capital debt repayment, reducing ongoing debt costs where possible.
- Utilising business rates volatility reserves and pooling gains to soften the impact of the expected fall in business rates retention funding to the Safety Net in 2022/23, when Hinkley B nuclear power station is decommissioned.
- Using general reserves flexibility developed during the past two years to soften the underlying budget gap in the short term.
- Maintain adequate contingencies and reserves to protect the Council’s ongoing

financial health and resilience to risk and uncertainty.

5.11 The Council set a balance budget for 2021/22 in February 2021. This included a planned allocation of £1.16m from general reserves to support the budget but also set aside significant contingencies and reserves to manage risk. As set out below, it is proposed to make a small number of changes to the 2021/22 budget through this report in respect of treasury costs, staff pay award and reserve transfers to support this updated strategy.

5.12 The updated MTFP (see section 6 below) includes an **estimated funding deficit (excluding reserve transfers) of £3.9m in 2022/23**. Table 1 sets out the proposed approach to mitigating the deficit and produce an indicative balanced budget in 2022/23. The MTFP and budget proposals will continue to be developed and refined through the year as estimates are updated for new information, therefore proposals and further options may be presented as the budget planning process progresses.

Table 1 – Draft Plans included in MTFP to Balance Budget in 2022/23

	2021/22 Budget £k	2022/23 Estimate £k
Proposed revision to 2021/22 Budget:		
Revised estimate – lower interest costs in 2021/22, through continued access to short term low cost debt to support commercial investment	-750	
Release funds from Business Rates reserve due to reduced risk	-1,250	
Transfer to Investment Financing Fund	2,000	
Investment Capital Debt repayment (MRP) reflecting 2020/21 outturn	80	
Investment Property Income increase in-year estimate	-80	
Measures included in 2022/23 estimates within MTFP:		
Planned use of general reserves to soften budget gap		-1,000
Transfer from Investment Financing Reserve to fund debt repayment		-2,000
Savings Target - modernisation, efficiency and improvement		-200
Proposed use of business rates reserves utilising historic pooling gains to maintain services and organisational capacity during transition to unitary structure.		-715

5.13 The inclusion of the above measures shows an early forecast of a potentially balanced budget in 2022/23, albeit **for <u>one year only with use of £3.7m one-off funding</u>**, as shown in the MTFP in section 7 below.

5.14 Utilising reserves to fund ongoing costs is **not financially sustainable in the long run**. This approach is regarded as prudent currently within the short term context of this strategy which protects services and capacity to support the transition to a unitary form of local government in Somerset up to March 2023. It is expected that further calls on reserves will be needed to fund unitary implementation costs however these are not currently built into the MTFP and are therefore currently unfunded.

6 Medium Term Financial Plan Estimates

6.1 The Medium Term Financial Plan (MTFP) was last set in February 2021 with the 2021/22 budget. The Council has set a balanced budget for 2021/22 with a forecast budget gap (deficit) of £3.5m in 2022/23. Assumptions and estimates have been updated since the February report, and indicative measures included in the plan to reduce the gap in 2022/23.

6.2 In view of the probable change in local government structure in Somerset from April 2023, the period covered by the MTFP is shorter within this report than in previous years with a focus on 2021/22 and 2022/23 for SWTC services, with an indicative forecast for 2023/24 costs based on a continuation of district council services in its current form for comparison.

6.3 Set out below is a summary of the updated MTFP. A reconciliation of the changes in the 2021/22 figures from the February 2021 budget report to this updated table is included in Appendix D.

Table 2 – General Fund Medium Term Financial Plan

	SWTC		New Unitary?
	2021/22 Revised Budget £k	2022/23 Estimate £k	2023/24 Indicative SWTC £k
Net Service Costs	21,020	21,934	21,916
Investment Properties Net Income*	-5,562	-7,157	-7,327
Capital Financing and Debt Repayment*	1,580	3,338	3,138
Interest Costs and Income*	323	416	1,169
Unparished Area Expenses	29	29	29
SRA Funding	98	98	99
Sub-total: Net Costs	**17,488**	**18,658**	**19,024**
Earmarked Reserves Transfers	2,415	-3,025	110
General Reserves Transfers	-1,160	-1,000	0
Net Expenditure	**18,743**	**14,634**	**19,134**
Business Rates Retention (BRR)	-6,182	-4,199	-4,281
BRR prior year surplus/deficit	12,556	1,331	1,331
Earmarked S31 Grant to offset BRR Deficit	-12,117	-999	-999
Business Rates Pooling Gain	-250	0	0
Revenue Support Grant	-6	-7	-7
Rural Services Delivery Grant	-253	-253	-253
LCTS Grant (COVID)	-225	0	0
Lower Tier Services Grant (COVID)	-996	0	0
New Homes Bonus	-1,743	-851	0
Council Tax (CT)	-9,490	-9,680	-9,971
CT Special Expenses	-29	-29	-29
CT prior year surplus/deficit	-8	53	53
Net Funding	**-18,743**	**14,634**	**14,156**
Budget Gap	0	0	**4,979**
Gap – Change on Previous Year	0	0	4,979

*To aid transparency and reporting, the cost of debt repayment and notional interest on investment properties is now included within total debt repayment and interest costs lines in the MTFP. This provides clarity on the extent of investment income and capital debt costs included in the MTFP. This was previously netted off investment properties income in the February 2021 budget report.

7 Service Costs and Income

7.1 The projections above reflect current estimates and prudent financial planning proposals incorporated within the Plan. The main assumptions included in respect of net expenditure include:

- Baseline expenditure budgets will continue in 2022/23, but the Directors and their management teams will continue to review and refine to reflect up to date need and trends.
- Staff pay awards are estimated at 1.5% in 2021/22, then 2% per year from 2022/23.
- Inflation increases incorporated for major contracts plus utilities and insurances.
- Employers pension contributions and Pension Fund deficit recovery lump sum costs based on the 2019 actuarial valuation.
- Savings in the leisure and waste contracts are fully delivered, albeit with a slight delay in the waste savings through Recycle More due to COVID.
- Fees and charges increasing by an inflationary amount like 2021/22, delivering an additional £100k per year.
- Balance of commercial property investment fund (Total Fund £100m) is fully invested by mid-2021/22.

8 Savings Targets

8.1 In the context of maintaining organisational capacity in the lead up and transition to a future model of local government in Somerset, short-term savings targets to be included in the financial strategy focus on modernisation, improvement and efficiency. A net savings target of £200,000 for 2022/23 is included within the MTFP forecast, as a realistic and achievable target.

8.2 Longer term savings and financial sustainability solutions for 2023/24 and beyond will need to be determined in the design and costing of a new unitary model, with significant financial benefits estimated within the future unitary options business cases. In the unlikely event a change to a unitary model is not agreed by the Secretary of State this year, SWTC will need to revisit the financial strategy and identify ongoing financially sustainable service options for future years.

9 Commercial Investment Strategy

9.1 The Council's Commercial Property Investment Strategy is reported in detail separately to Council. This commercial approach responds to the major cuts in central government funding and reduction in retained business rates income, to provide essential income to fund local services. It also provides a prudent diversification of funding streams, where reliance on business rates growth, New Homes Bonus and general grant funding is not sustainable.

9.2 The last update of the Strategy was approved by Council in December 2020. Effective governance and management arrangements provide confidence over the financial assumptions supporting the strategy, with realistic estimates included in the MTFP. The programmed investment of £100m in property commenced in 2020/21 and is expected to be completed in 2021/22.

9.3 The acquisition of investment properties will initially be funded through borrowing – either through internal borrowing or external financing facilities such as loans – with debt acquired in line with the Treasury Management Strategy. Interest rates on borrowing are expected to remain low in the medium term.

9.4 The presentation of investment income has been updated within the MTFP, showing investment income net of direct management costs, with financing costs included within Capital Financing and Debt Repayment, and Interest Costs and Income.

9.5 Investment risk is managed through robust governance, due diligence, and ongoing effective management of the portfolio. Budget risk is underwritten through prudent estimating of return on investment and holding an Investment Risk earmarked reserve that provides significant resilience to income volatility and asset management costs. It is proposed to split the earmarked reserve into three specific reserves in 2021/22 including the creation of an investment financing reserve to hold surpluses that may be used to finance capital costs and/or accelerate debt repayment. Estimates of reserve transfers and balances are set out in Appendix A.

Table 3 – Investment Property Net Income Estimates

	2021/22 £k	2022/23 £k	2023/24 £k
Net Income from Investment Assets Transferred from TDBC and WSC	-507	-507	-507
Net Income from £100m investment portfolio	-4,975	-6,650	-6,820
Net Income from £100m (21/22 revised estimate) reduced optimism adjustment contingency	-80		
Total Investment Properties Net Income	**-5,562**	**-7,157**	**-7,327**
Related Financing Cost Estimates:			
Capital Debt Repayment Estimates	800	2,000	2,000
Capital Debt Repayment (21/22 Revised Estimate)	80		
Notional Interest Costs	1,275	750	1,500
Notional Interest Costs (21/22 Revised Estimate)	-750		
Estimated Net Income After Financing Costs	**-4,237**	**-4,407**	**-3,827**

9.6 Significant progress in the delivery of the investment strategy has been made in 2020/21 and Q1 of 2021/22. Given increasing confidence with net income projections the investment income in 2022/23 has been enhanced by £250k with reduction in the ‘optimism adjustment’ contingency within the budget estimate. This enables a reduction in the use of General Reserves towards the cost of services in 2022/23.

9.7 The presentation of the MTFP has been updated to show investment properties net income before financing. This helps to provide further clarity for councillors on the extent to which investment income supports the cost of services, and the total debt repayment and interest costs included in budget estimates. It also reflects the financing of investment property capital is managed by the S151 officer in line with the treasury management approach required to meet the Council’s total capital requirements which is undertaken on a holistic basis.

10 Regeneration

10.1 The Council has strategic plans to drive forward with regeneration within the district. For example, Seaward Way (Minehead) employment site development completed in 2020/21, the Coal Orchard (Taunton) development will complete in 2021/22, and work is continuing at the Firepool site (Taunton). These regeneration schemes are addressing market failure and improving the place and are also expected to provide a net income towards related services through robust viability planning and cost management. Where the Council retains an ongoing interest in a completed site the budget will reflect known costs and income estimates. The net cost/income for regeneration schemes will be driven by quality and cost of the schemes, the delivery and financing arrangements, and nature of income.

11 Treasury Management and Capital Financing

11.1 The Council updates its Treasury Management Strategy (TMS) annually, with the current TMS approved by Full Council in March 2021. The strategy guides the approach to managing the Council's cash flow, cash investments and borrowing.

11.2 The current economic outlook has several key treasury management implications:

- Short term investment returns are likely to remain relatively low
- Borrowing interest rates are currently attractive and are likely to remain low for some time
- Financial markets suffered significantly during 2020/21 due to COVID impact on the economy, but are beginning to bounce back as restrictions are eased, underpinned by the successful vaccinations programme.
- Approaches to financing capital investment plans should consider the economic outlook e.g. any potential advantages of taking more long term borrowing to increase cost certainty and reduce interest rate risk.

11.3 This TMS looks to manage exposure to risk and volatility by:

- Considering security, liquidity and yield, in that order
- Considering alternative assessments of credit strength
- Spreading investments over a range of approved counterparties
- Only investing for longer periods to gain higher rates of return where there are acceptable levels of counterparty risk
- Only borrowing when needed and managing borrowing undertaken to prudently reflect a balance of short term low cost debt, long term cost certainty, and retaining flexibility of arrangements in view of the range of uncertainties and dynamic capital programme requirements.

11.4 The S151 Officer and Finance staff continue to work with our treasury advisors – Arlingclose – to effectively manage opportunities and risks in line with CIPFA's Prudential Code and Treasury Management Code and related Guidance.

11.5 The cost assumptions in respect of interest in debt for 2021/22 and 2022/23 have been reduced in the MTFP on the assumption we will continue to access short term external borrowing to support General Fund capital expenditure where needed. This assumption reflects forecasts provided by Arlingclose that interest and borrowing rates are not expected to change materially in the next 2-3 years. This builds in an element of risk in terms of refinancing costs in future however for the duration of this strategy the risk is low.

12 Reserves

12.1 The Council maintains General Reserves and Earmarked Reserves, for both the General Fund and the Housing Revenue Account. General Reserves are retained to provide a contingency to mitigate general financial risks arising from unexpected events or emergencies and as a general working balance to help cushion the impact of uneven cash-flows. Earmarked Reserves are funds that have been set aside for specific purposes to be spent in future years and to provide contingencies for specific risks. The approach to General Reserves includes a regular review by the S151 Officer to ensure the level of reserves held are adequate in the context of the financial risks faced and other mitigations in place (e.g. provisions, earmarked reserves, insurances).

12.2 The Council currently holds a balance above the recommended minimum, and a key principle within this financial strategy is that it is prudent to maintain and where possible to increase this headroom to ensure revenue resources are available to support the implementation of a new unitary structure if approved. For example, the Stronger Somerset business case identifies estimated implementation costs of £18.9m. In addition, proportionate contingencies are in place for 2021/22 however long lasting COVID effects on the economy, demand for services and income levels increases financial planning risk, and higher reserves 'headroom' provides greater resilience in this context.

12.3 This financial strategy includes planned use of surplus general reserves to support the budget in 2021/22 (£1.16m) and 2022/23 (£1m). This is reflected in the MTFP above and is sustainable in the short term. Sustainable financial planning must ensure that in the medium/long term the budget can be balanced without the need to use General Reserves.

12.4 The Council sets aside funds into Earmarked Reserves through the Budget process where there is a longer term spending plan, for example planned use of revenue funds towards financing the capital programme, and Business Rates which mitigates financial risks and smooths out accounting timing differences. A review of reserves was undertaken in 2020 in response to COVID and reflected within plans for 2020/21 and 2021/22. A further review of earmarked reserves will be undertaken this summer and reported to Members in due course.

12.5 For this updated Financial Strategy and budget approach it is proposed to further realign reserves to reflect up to date risk assessments, and plans to utilise investment, financing and business rates surpluses to support the investment property strategy in 2021/22 and 2022/23. This is as set out in Table 1 above.

12.6 A summary of the general reserves and earmarked reserves position is set out in Appendices B and C.

13 Business Rates Retention (BRR)

13.1 The Council's business rates tax base includes Hinkley Point nuclear power station, with Hinkley B representing almost 20% of the total. EDF have confirmed that Hinkley B will commence decommissioning by July 2022, which has a major influence on retained business rates funding for SWTC. From 2022/23 it is projected that BRR funding will fall to the Safety Net retained funding c£4.2m, a significant reduction of approximately £2m per year compared to 2021/22. It is unlikely BRR funding would return above the Safety Net until Hinkley C is operational, which is not expected to be before 2026/27.

13.2 The Council has been preparing for the prospect of reduced business rates from Hinkley B by building resilience in its BRR Volatility Reserve. With the expected reduction in 2022/23 it is proposed to use part of the reserve balance to mitigate the reduction in funding. This allocation is currently estimated at £0.5m but the amount will be confirmed within the final Budget proposal in February 2022.

13.3 The anticipated review of the Business Rates Retention (BRR) system and the “Reset” of the Baseline has been deferred several times by Government, and at this stage it is unclear when this will happen. However, the impact of this prospective change may be less significant in the medium term due to Hinkley B decommissioning, although it may depend on what data the Government uses to inform any reset.

13.4 The Government announced last July that the next revaluation of rateable values would be in 2023 with an Antecedent Valuation Date (AVD) of 1 April 2021, which would reflect the impact of COVID-19 on the non-domestic property markets. The Non-Domestic Rating (Lists) Act 2021 came into force in March, setting the publication date of the compiled lists (1 April 2023) and the publication of the Draft Lists to be no later than the 31 December 2022. The 2023 revaluation will require the Valuation Office to carry out in the region of 2.12 million valuations.

Business Rates Pooling

13.5 A Somerset Business Rates Pool (comprising the County Council and the Districts within the County Council area) has provided a positive impact on retained funding since 2018/19, retaining more funding locally rather than redistributed to central government. The pooling arrangement remains in place for 2021/22. The 2021/22 Budget includes an estimated £250k pooling gain as a contribution towards funding of services. Actual gains are not confirmed until the end of each financial year.

13.6 In the overall context of the financial strategy, it is proposed that pooling gains from 2020/21 (estimated £0.9m) and any additional surplus in 2021/22 is reserved to support the budget in 2022/23 and additional financial sustainability measures such as capital financing.

13.7 With the planned decommissioning of Hinkley B nuclear power station in 2022 it is unlikely that SWTC would continue in any pooling arrangement in 2022/23, however this will be reviewed later this year with a decision for 2022/23 due in October.

14 Business Rates Holiday 2020/21 and Collection Fund Deficit

14.1 One of the measures introduced in response to COVID and to support businesses is to give a one-year business rates holiday to eligible businesses in the retail, hospitality and leisure sector plus Early Years nursery providers in 2020/21. This has resulted in a £29m reduction of business rates due from rate payers. As businesses are paying less this results in a significant deficit in the Collection Fund of which SWTC is liable for 40%.

14.2 The Government is providing S31 grant to compensate local authorities for the loss of tax revenues through the business rates holiday. There is a timing difference in the prescribed accounting arrangements in that the General Fund will be credited with the S31 grant in 2020/21 but the Collection Fund deficit is charged to the General Fund in the following financial year. This means the budget estimates and reserve balances are significantly skewed. It is important to set aside the S31 grant in the Business Rates Volatility Reserve in 2020/21 and then withdraw it later to offset the deficit when this hits the General Fund.

15 General Government Grants

15.1 Budgeting for General Grant funding is uncertain and subject to future Spending Reviews and the annual Finance Settlement. Currently the funding forecasts within the MTFP are based on a continuation at the same cash values for both Revenue Support Grant (RSG) and Rural Services Delivery Grant (RSDG), totalling £260k per year (see MTFP summary in Table 2 above).

15.2 The prospect of a reduction in funding through a 'negative RSG' has been postponed each year for several years by Government, therefore no allowance for this is currently included in the forecast pending future Government announcements in this regard.

16 New Homes Bonus

16.1 New Homes Bonus grant provides additional un-ringfenced funding from Government based on annual housing growth. The scheme has been in operation since 2011/12, with various changes to the methodology for calculating the grant during this time. The Government has undertaken a further consultation on the future of New Homes Bonus in early 2021, and it is likely information will come forward later this year (December?) on any changes being implemented. At its peak NHB funding within SWT reached £4m, but the level of reward has diminished year on year since.

16.2 The reward for the previous year's annual growth within the 2021/22 settlement was £34k which combined with legacy payments of £1.709m from prior years' growth resulted in a grant of £1.743m in 2021/22. The legacy payment due on 2022/23 is £851k and it is currently assumed this will be the total NHB funding received in that year, which is all planned to be used to support the revenue cost of services. If the Finance Settlement confirms a higher grant amount in 2022/23 it is proposed to reduce the amount required from reserves to balance the budget.

16.3 The expected reduction in availability of New Homes Bonus has led to a review of the affordability and funding of the Growth Capital Programme – see para 21.9 below.

17 Council Tax

17.1 The setting of Council Tax is determined by Members each year at Full Council. For 2021/22 the Council set the basic annual Band D council tax rate for Somerset West and Taunton Council at £169.63 (including £1.75 which is passed on to the Somerset Rivers Authority). The Tax Base – the measurement of properties chargeable for tax expressed as 'Band D Equivalents' – is 55,948 in 2021/22.

17.2 This produces council tax income of £9.49m for SWTC, which represents 51% of Net Funding within the 2021/22 revenue budget.

17.3 The council tax income projections within the MTFP are based on the financial planning assumption of a 1.99% annual increase in council tax rate. The Government has for several years allowed shire districts the option of up to a £5 increase on the Band D rate, if this is greater that 1.99%. If this option is available and taken in 2022/23 this would equate to 2.94%. Tax proposals will be considered by the Executive through the budget process, and formally recommend its Council Tax proposals to Council each February as part of the annual Budget report.

17.4 The impact of COVID on the local economy and employment is expected to have an ongoing adverse effect on council tax income. No growth in the tax base is assumed in 2022/23, recognising the risk that any housing growth will be offset by increased demand in council tax support.

17.5 In the 2021/22 Finance Settlement the Government provided a one-off grant of £225k to mitigate the increased demand in council tax support. It is not known whether any further mitigation funding will be provided in 2022/23, therefore prudently no further funding is currently anticipated within the MTFP.

17.6 The table below provides a summary of the assumptions and estimates included the MTFP projections. If there is a new unitary structure in 2023/24 a council tax harmonisation approach will need to be agreed for SWTC's successor.

Table 4 – Council Tax Income Forecast

	2021/22 Actual	2022/23 Estimate	2023/24 Indicative
Council Tax Base			
Estimated Increase/Decrease %	-0.9%	0%	1%
Increase/Decrease in Band D Equivalents	-502	0	560
Tax Base	55,948	55,948	56,507
Council Tax Rate			
Increase % (MTFP core assumption)	3.07%	1.99%	1.99%
Increase £	5.00	3.38	3.44
Band D Rate £	169.63	173.01	176.45
Council Tax Income Estimates £k	**9,490**	**9,680**	**9,971**
Council Tax Income scenarios £k: £5 annual increase 1% annual increase 0% annual increase		 9,770 9,585 9,490	 10,150 9,777 9,585

18 Somerset Rivers Authority

18.1 Included in the Council Tax Band D tax rate for SWTC is £1.75 per year which is collected by SWTC on behalf of the Somerset Rivers Authority (SRA). This equates to an estimated £98k in 2021/22, providing funding towards the 20 Year Flood Action Plan that was developed following the severe flooding experienced in Somerset in early 2014. Total contributions from the County and District Councils in Somerset provide an annual budget for the SRA of c£2.8m per year. There are five key workstreams within Somerset's 20 Year Flood Action Plan:

- dredging and river management
- land management (including natural flood management)
- urban water management
- resilient infrastructure
- building local resilience

18.2 The Government has previously committed to implementing the necessary legislation in future to allow the SRA to precept.

19 Housing Revenue Account

19.1 The Housing Revenue Account (HRA) is a ring-fenced, self-financing account where income from tenants and sale of assets funds the homes and related services provided to tenants, and investment in the provision and quality of council owned housing stock.

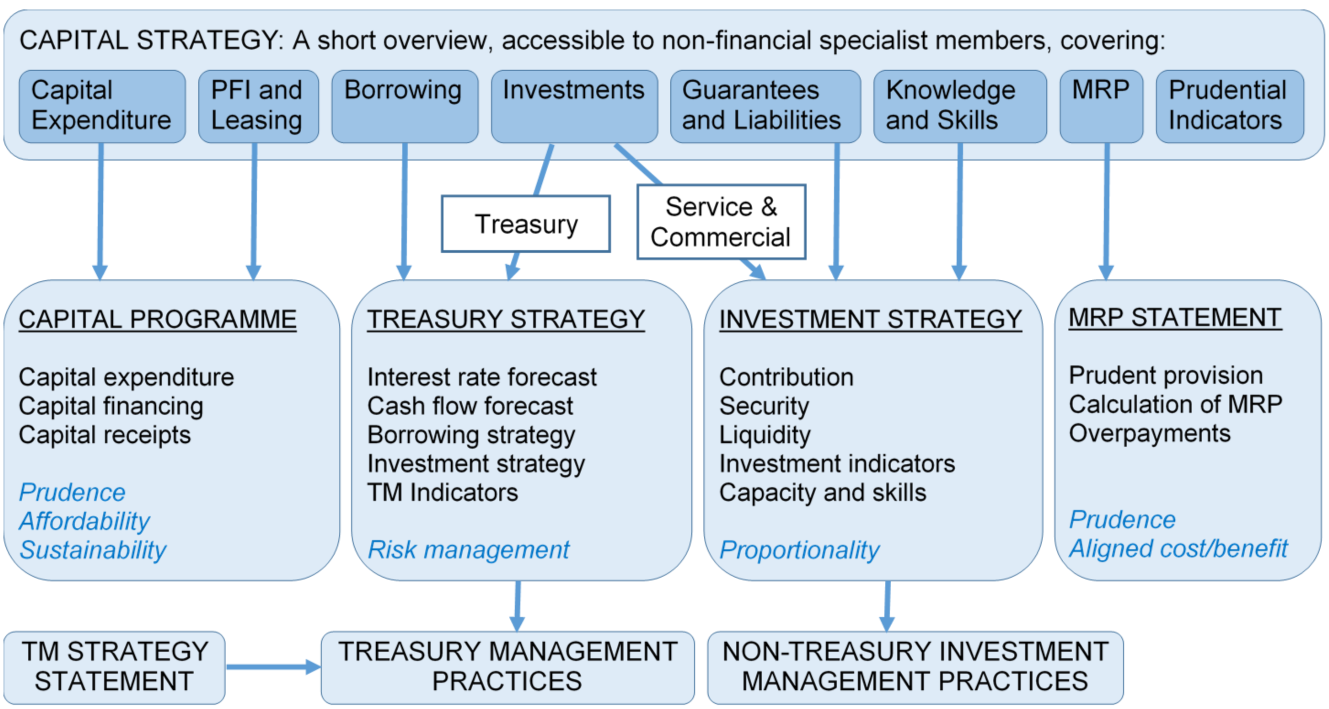
19.2 The Council has a long term business planning approach to managing the stock and the finances within the HRA, which is reported separately. The financial strategy for the HRA focusses on ensuring that spending and capital investment plans are affordable and contained within the projected resources available.

19.3 The Council maintains separate reserves – general and earmarked – for the HRA representing balances and contingencies to manage financial risks and timing of spending commitments.

20 Capital Strategy

20.1 The Council approved new Capital, Investment and Treasury Strategies in February 2021. These draw together the approaches to meeting the Council's capital investment priorities, and managing its investment, borrowing and cash flow needs and risks.

20.2 The strategy follows the principles of the Prudential Code and Treasury Management Code issued by CIPFA. The following diagram represents the Capital Strategy framework and how the capital, investment, treasury and MRP approaches interlink.



20.3 The key objective of the Capital Strategy is to deliver a capital programme that:

- Ensures the Council's capital assets are used to support the delivery of priorities within the Corporate Plan and the Council's vision
- Links with the Council's Asset Management Plan

- Is affordable, financially prudent and sustainable
- Ensures the most cost effective use is made of existing assets and new capital investment
- Supports other service specific plans and strategies

20.4 For the General Fund the majority of direct service investment is supported through use of New Homes Bonus funding and Community Infrastructure Levy; with further investment supported through planning obligations (S106/Hinkley funds), capital grants, capital receipts, and revenue contributions. For the HRA the funding is provided through the Major Repairs Reserve, capital receipts and revenue contributions. A contribution to the Social Housing Development Fund is included in the HRA Revenue Budget each year to contribute towards the cost of additions to the housing stock.

20.5 For both the General Fund and HRA, future capital spending will require support through borrowing. Prudent borrowing limits will be set within the Capital and Treasury strategies, together with prudent plans to cover the cost of capital debt through Minimum Revenue Provision (MRP) and use of capital receipts. The revenue implications of capital will be measured for affordability within the overall revenue budgets for the General Fund and HRA.

20.6 The specific resources to deliver the capital strategy will be identified through the annual budget setting process. The Council will use a rigorous capital prioritisation process before individual capital schemes are approved including development of a full business case for large individual capital schemes.

Infrastructure Programme and Community Infrastructure Levy

20.7 The Council applies a Community Infrastructure Levy (CIL) for relevant development within the district, in line with the policy originally introduced by Taunton Deane Borough Council in 2014. CIL is a tariff charged in the Taunton Deane area on residential development (excluding Taunton town centre and Wellington) and retail development outside Taunton and Wellington town centres. The principle behind CIL is that most development has some impact on infrastructure and the developer should contribute to the cost of providing or improving it. CIL applies to new floor space and charges are based on the size, type and location of the new development.

20.8 The Policy is approved by Council and implemented by Officers. Council determines the allocation of CIL income to investment themes as part of the annual capital programme approval process. The Executive Committee or Portfolio Holder for Asset Management and Economic Development may agree specific scheme allocations for projects >£250k, or the External Operations and Climate Change Director for projects up to £250k, within the limits allocated by Council to each theme. Expenditure to be funded by CIL is only contractually committed once CIL income has been received.

20.9 Detail regarding planned CIL allocations to support expenditure is set out in the approved Capital Programme.

21 Financial Planning Risks and Uncertainty

21.1 As outlined in this report, there are number of factors making accurate financial forecasting particularly difficult at this stage. The risk of 'error' in forecasting assumptions is high, particularly for 2021/22 onwards. The financial strategy seeks to mitigate this risk by:

- Prudent assumptions used for future funding forecasts
- Maintenance of sufficient balances and reserves

21.2 Other main areas of risk and uncertainty within the financial plan are:

- Inflation – rising inflation could place additional pressure on pay settlements and prices for purchases of goods and services
- Demand volatility – fluctuation in costs and income as a result of changes in demand led services and usage (e.g. homelessness, planning, building control, parking, garden waste), which may continue to be adversely affected by COVID.
- Delivery of savings – planned savings to mitigate the projected budget gap may take longer to be delivered and may not be delivered in full, in which case plans will need to be reviewed and updated.
- Business Rates Retention – forecasts under BRR are notoriously difficult to predict with accuracy and can therefore change from year to year (e.g. for appeals, reliefs, etc.), and the system is currently under review with uncertainty of the distribution of risks and rewards of income decline and growth.
- Economic slowdown and recession – COVID and exit from the EU may exaggerate the impact on demand for services thus increasing costs, and is expected to have an adverse effect on core funding through business rates and council tax as well as income from fees and charges.
- Local government – The Government is currently considering two options for local government restructuring in Somerset, with the potential for one or two unitary councils taking on the services currently delivered by the County and District councils. Any change is likely to have a significant demand on resources to manage a transition to a new authority, leading to increased costs and potentially significant reductions in reserves.

22 Legal Implications

22.1 The Council is required by law to set a balanced budget and failure to do so would result in serious financial and service implications and lead to Government intervention.

23 Climate and Sustainability Implications

23.1 No direct carbon/environmental impacts arising from the recommendations. Budgeted support towards the Council's climate and sustainability priorities is included within the MTFP and HRA Business Plan.

24 Equality and Diversity Implications

24.1 No direct equality or diversity impacts arising from the recommendations within this report. Officers and members will need to consider whether there are any impacts for detailed policy updates and proposals within the detailed budget plans as these are developed and presented for decision.

25 Asset Management Implications

25.1 Effective asset management remains an important element of the financial strategy. Asset Management Strategies were previously prepared for both West Somerset and

Taunton Deane Councils (September 2017 and November 2017). These identify and categorise the land and property holdings in each Council and establish core objectives for holding and/or investing in the existing asset base. Work is currently underway to enable updated Asset Management Plans to be prepared during 2021/22. Financial plans will be reviewed and budgets updated during the budget setting cycle to reflect updated information when available.

26 Scrutiny Comments / Recommendations

26.1 It is proposed to present the draft strategy to Scrutiny on 7 July 2021. Feedback from the Committee will be included in the report to the Executive on 21 July 2021.

Democratic Path:

- **Corporate Scrutiny Committee – 7 July 2021**
- **Executive – 21 July 2021**
- **Full Council – 7 September 2021**

Reporting Frequency: Annually

Appendices

Appendix A	Investment earmarked reserves
Appendix B	General Reserves summary
Appendix C	Earmarked Reserves summary
Appendix D	Reconciliation of 2021/22 MTFP Budget Changes Since February 2021

Contact Officers

Name	Paul Fitzgerald
Direct Dial	01823 217557
Email	S151@somersetwestandtaunton.gov.uk
Name	Emily Collacott
Direct Dial	01823 218742
Email	e.collacott@somersetwestandtaunton.gov.uk

Appendix A

Investment Earmarked Reserves

Table 1 – Investment Risk Reserve Projection

	2021/22 £k	2022/23 £k	2023/24 £k
Balance brought forward	3,674	3,000	3,000
Transfers to other Investment Reserves	-674	0	0
Transfer to reserve (MTFP assumption)	0	0	320
Transfer to Revenue – determined by future volatility	TBC	TBC	TBC
Balance carried forward	3,000	3,000	3,320

Table 2 – Investment Assets Sinking Fund Projection

	2021/22 £k	2022/23 £k	2023/24 £k
Balance brought forward	0	500	500
Transfer from Investment Risk Reserve	500	0	0
Transfer to Reserve – set aside from Investment Net Income	0	0	100
Transfer to Revenue – asset maintenance/management costs	*TBC*	*TBC*	*TBC*
Balance carried forward	500	500	600

Table 3 – Investment Financing Reserve Projection

	2021/22 £k	2022/23 £k	2023/24 £k
Balance brought forward	0	2,174	174
Transfer from Investment Risk Reserve	174	0	0
2021/22 Revised Budget – Transfer to reserve	2,000	0	0
Repayment of Investment Capital Borrowing (MRP)	0	-2,000	0
Balance carried forward	2,174	174	174

Appendix B

General Reserves

Reserves Position as at July 2021

	General Fund £k	HRA £k
Balance 1 April 2020	**4,522**	**2,701**
2020/21 Original Budget Transfer to Reserve	300	
Earmarked reserves review – balances released	1,218	
From NHB Reserve	3,949	
From BR Volatility Reserve	1,000	
Economic Growth and Prosperity Fund	-500	
Climate Change strategy	-500	
Unitary Programme Delivery Funds	-249	
Tree Planting	-18	
2020/21 Budget for Projected Net Costs of COVID	-657	
Budget Volatility and Risk reserve	-2,400	
2020/21 Outturn Net Underspend (Overspend)	1,250	15
Balance 31 March 2021	**7,915**	**2,686**
Requested Supplementary Budgets 2021/22 (Outturn report)	-806	
MTFP Use of Reserves to Reduce Budget Gap in 2021/22	-1,160	
MTFP Use of Reserves to Reduce Budget Gap in 2022/23	-1,000	
Unitary Council Poll	-86	
Indicative Balance	**4,863**	**2,686**
Adequate Minimum Reserves Balance	2,400	1,800

Appendix C

Earmarked Reserves

General Fund Earmarked Reserves	Balance 1 April 2021 £k	Budgeted Transfer £k	Balance 31 March 2022 £k
Business Rate Holiday S31 Grant	11,695	-11,118	577
Business Rate Losses S31 Grant	3,081	-999	2,083
Business Rate Volatility	5,375	1,665	7,040
Investment Risk	3,673		3,673
Budget Volatility & Risk	2,400		2,400
General Carry Forwards	2,112	-2,112	0
Garden Town Fund	870	-68	802
Ec Dev (BR Pooling Gain)	769		769
Asset Management	687		687
Community Housing (West Som)	533		533
NHB	193		193
Other Smaller Balances	2,456	-18	2,438
Total	**33,844**	**-12,649**	**21,194**

**Excludes proposed transfers in Table 1 in this report.*

HRA Earmarked Reserves	Balance 1 April 2021 £k	Budgeted Transfer £k	Balance 31 March 2022 £k
HRA One Teams	26		26
HRA Social Housing Development Fund	849		849
HRA Hinkley	57		57
HRA Contribution to Transformation	175		175
Total	**1,107**	**0**	**1,107**

Appendix D

Reconciliation of movements in 2021/22 figures in MTFP Feb Council to this report

	2021/22 February Report £k	Changes £k	2021/22 This Report £k
Net Service Costs	21,020		21,020
Investment Properties Net Income	-3,407	-2,155	-5,562
Capital Financing and Debt Repayment	498	1,082	1,580
Interest Costs and Income	Not split out	323	323
Unparished Area Expenses	29		29
SRA Funding	98		98
Sub-total: Net Costs	**18,238**	**-750**	**17,488**
Earmarked Reserves Transfers	1,665	750	2,415
General Reserves Transfers	-1,160		-1,160
Net Expenditure	**17,993**	**750**	**18,743**
Business Rates Retention (BRR)	-6,182		-6,182
BRR prior year surplus/deficit	12,556		12,556
Earmarked S31 Grant to offset BRR Deficit (split over two lines in February report)	-12,117		-12,117
Business Rates Pooling Gain	-250		-250
Revenue Support Grant	-6		-6
Rural Services Delivery Grant	-253		-253
LCTS Grant (COVID)	-225		-225
Lower Tier Services Grant (COVID)	-996		-996
New Homes Bonus	-1,743		-1,743
Council Tax (CT) (SRA element split out in Feb report)	-9,490		-9,490
CT Special Expenses	-29		-29
CT prior year surplus/deficit	-8		-8
Net Funding	**-18,743**	**0**	**-18,743**
Budget Gap	**0**	**0**	**0**

Brief explanation of changes:

1. Investment properties net income: £750k reduction in financing interest costs improving net income, MRP increased by £80k offset by £80k increase in net income, £880k MRP moved to ‘Capital Financing and Debt Repayment’ line, £525k interest costs moved to ‘Interest Costs and Income’ line.

2. Capital financing and debt repayment: £202k interest income moved to ‘Interest Costs and Income’, £880k MRP moved from ‘Investment Properties Net Income’.

3. Interest costs and income: -£202k net interest income split out from original budget, £525k interest costs moved from ‘Investment Properties Net Income’.

4. Earmarked reserve transfers: £750k interest cost reduction transferred to Investment Financing Fund. Also £1.25m transferred from BRR Volatility Reserves and subsequently also transferred to Investment Financing Fund, making £2m in total to that Fund.