Cambridgeshire County Council

Appendix 3

Draft

Medium Term Financial Strategy

2022-2023

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Extract

Contents

Section 1 - Executive summary

The Council's strategic financial framework is comprised of three distinct, but interdependent, strategies set out within this Business Plan:

- Medium-Term Financial Strategy (MTFS) (Section 2)
- Capital Strategy (Section 6)
- Treasury Management Strategy (Section 7)

This Strategy sets out the financial picture facing the Council over the coming five years, the resources available to the Council, and the Council's strategy for managing its resources effectively.

As well as outlining the Council's revenue strategy, this Medium-Term Financial Strategy includes the organisation's Fees and Charges Policy and Reserves Policy.

The ongoing effects of the COVID-19 pandemic, the economic picture, and government reforms continue to make forward planning with any degree of certainty extremely challenging. Medium-term planning in the first part of 2021-22 saw our projected budget shortfall in 2022-23 rise to £23m as a result of expected increases in demand for services and inflationary costs, as well as specific service pressures, and our budget gap over the five-year medium-term rise as well. At the same time, there is a need to invest in some services to improve outcomes, and to delivery longer-term sustainability or financial benefit.

The longer-term impacts of COVID-19 are expected to extend considerably into the MTFS period. Some of the specific challenges that the Council expects to face over the next five years are:

- Potential for growing regional and more local inequalities as a result of the economic fallout from the pandemic
- Ongoing lower levels of fees and charging income, as well as reduced local taxation receipts
- Uncertainty about the need for, and funding for, lasting COVID-19 related costs such as personal protective equipment or infection control procedures in social care providers
- Providing additional support for our local care markets to ensure sufficient appropriate care provision remains available

In June 2019, the Government legislated for reaching net zero carbon emissions by 2050, and locally the Council's joint administration has put responding to the climate emergency at the centre of our priorities. Meeting this commitment will require a transformation of our procurement practices for a greener future and investment into low carbon technologies, services and infrastructure supported by innovative green investment models.

There is a great deal of uncertainty surrounding the UK's public finances. In December 2020 the UK secured a post-Brexit trade deal with the EU, however the medium-term impacts of the new trading arrangements on economic growth, labour availability, and the cost of goods and services are still unclear and may yet influence levels of resources available to local authorities. Short-term disruption, particularly shortages of labour and materials, has increased costs for the Council. In addition to the international uncertainty, there are a number of Central Government reforms currently expected or that have paused, most notably those on technical aspects of Fair Funding and the Business Rates Retention Scheme, which are expected to affect the Council's funding, as well as the reforms of Adult Social Care. The outcomes of any announcements or associated consultations will be taken into account within the Business Plan as they become available.

The Fair Funding Review will affect how funding is allocated and redistributed between local authorities. It will reset business rate baselines which set out expected business rate receipts, funding baselines which determine relative need, and the tier split of business rates between County Councils and District Councils. The Government's preferred option is for a per-capita foundation formula with seven service-specific funding formulae and an Area cost Adjustment to reflect the differences in the cost in delivering services in different areas of the country. Damping is expected to play a significant role in limiting reallocations of funding between local authorities. It is also likely that reallocations will be phased in so no local authority will face a cliff edge cut to their funding or a step change increase in their funding. The future funding model for Local Government will need to support investment into mitigating and adapting to climate change and recognise that the scale of investment required to address this challenge will vary considerably across the country due to housing densities, rural transport, agriculture and other considerations.

Cambridgeshire has one of the fastest growing populations in the country and, as such, we are under particular pressure as the number of people accessing our services increases. The general population is also aging due to increasing life expectancies which is putting pressure on the ability of service users to contribute to the long-term costs of their care. In addition to this background population growth, the needs of those requiring care packages are becoming more complex and therefore costly. The uncertainty around this has been increased by the government's proposed reforms to care funding, both in terms of implementation timescales and the funding that will be made available to local government. As a result, the Council will work increasingly across service, organisation, and sector boundaries to find ways in which the resources of the wider public sector and the community can be best used to achieve the outcomes we strive for in the context of a rapidly increasing number and need of local population. The same applies for addressing the climate emergency and transforming to a low carbon economy - joined up action and policy across the wider public sector, business and the communities is needed to achieve the Government's net zero carbon emissions target by 2050.

In balancing our budget, some service reductions are inevitable, and we will always focus on reforming services or bringing in additional income rather than cutting services within this approach. The Council will seek to shape proposals so that the most vulnerable are the least affected. The Council has a statutory responsibility to set a balanced budget each financial year and the proposals that are already within the Business Plan for 2022-27 do contain some proposals that reflect considerable risk and uncertainty. This strategy sets out the issues and challenges for the next five financial years and creates a framework within which the detailed budgets will be constructed.

The key elements of this Strategy, on which basis the Business Plan is predicated, are set out below:

- Strategy & Resources Committee and Full Council will consider an updated approach to Council Tax levels in due course
- An assumed increase in the tax base of 2% for council tax, and variably by district for business rates
- The strategic approach to closing budget gaps to support the business plan will continue to evolve, focussing on reducing demand for our services, increasing income, decentralisation, finding efficiency and maintaining a medium-term outlook
- Funding for invest to save schemes or for service reform will continue to be made available through reserves, or capital where appropriate, subject to robust business cases
- The general reserve will be held at 4% of non-schools expenditure, and we will adopt a prudent approach in our reserves strategy to offsetting risks faced by the Council
- Staff pay inflation has been assumed to be 2.00% across all years of the medium-term, other than the expected rise at the lower end to keep pace with the real living wage
- Fees and charges will be reviewed annually in line with the Fees and Charges Policy
- The capital programme will be developed in line with the framework set out in the capital strategy, and the level of prudential borrowing by the Council over the medium-term will be reviewed
- Opportunities for cross-sector and organisational working that drive end to end efficiencies and/or improvements in service delivery will be pursued;
- Business rates pooling will be fully explored with district councils and the Combined Authority where there is a mutual financial benefit to do so;
- The Council Tax assumption and forecasts are reviewed annually
- The Council will continue to lobby central government for fair funding leading into the national replacement of the current funding formula.

The Council’s budget is divided into four main service blocks, and it is in these blocks that detailed budgets are shown in Section 3 of the business plan:

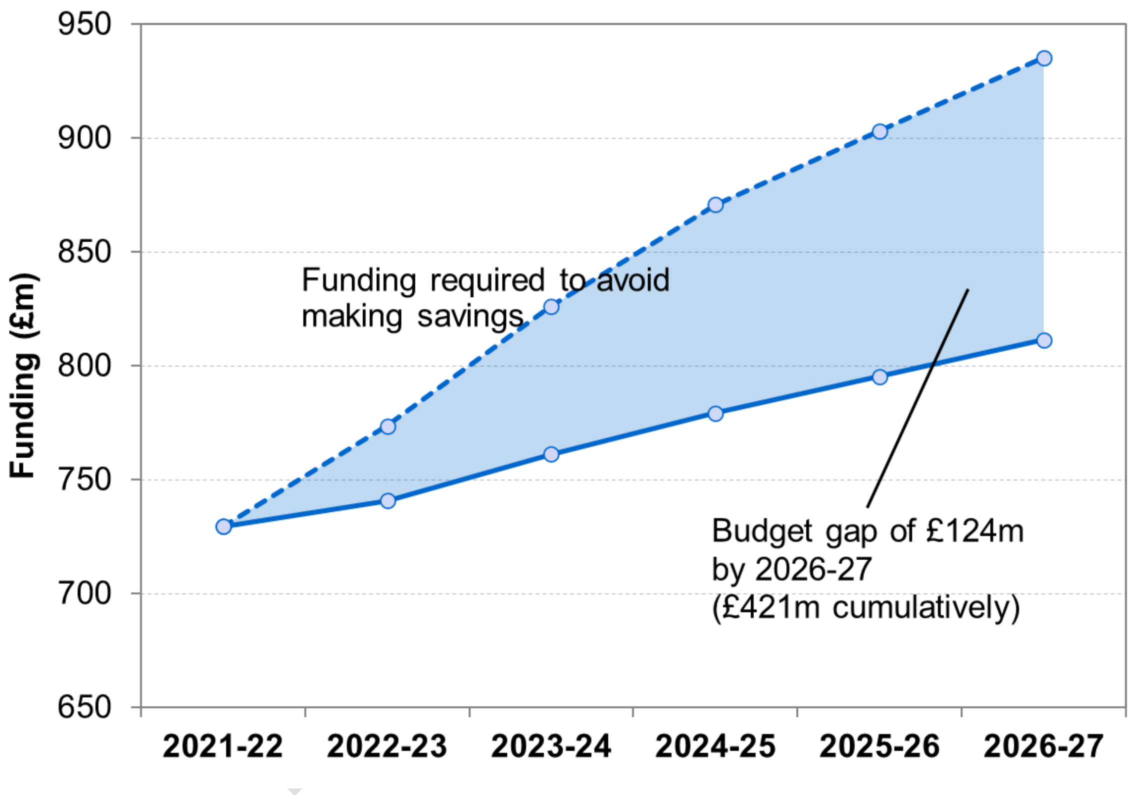
- People and Communities
- Public Health
- Place and Economy
- Corporate Services

Section 6 - Revenue Strategy: Balancing the budget

Every local authority has a legal responsibility to set a balanced budget every year. It is the Chief Finance Officer's statutory responsibility to provide a statement on the robustness of the budget proposals when they are considered by Council.

Inevitably, cost pressures are forecast to outstrip available resources, given the rising costs caused by inflation, growth and associated demand pressures and renewed pressure on levels of funding for local government in the wake of the pandemic. Consequently, we will need to make significant further savings, or generate significant additional income, to close the budget gap.

Figure 6.1: Current Budget gap before savings/income



Closing this budget gap over the next five years will mean making tough decisions on which services to prioritise. Some savings or additional income are already included in the draft business plan that partly close this gap.

During the last few years, services have made significant savings through increasing efficiency and targeting areas that are not our highest priority with the aim of minimising the impact on our service users.

We now face demand pressures that are increasing year-on-year faster than expected, as well as an uncertain economic outlook. We must also, however, invest in services that can bring the most benefit and reduce cost pressures over the longer-term.

Savings to be made from incremental efficiencies are likely to be minimal as we have had reducing government funding and cost pressures for over a decade. The easy savings have mostly been made. We must therefore focus on reviewing any service areas where we can disinvest, drive more innovative and transformative change across the medium-term, and maximise the income that can be generated locally.

We are currently awaiting a medium-term funding settlement for local councils given by central government, which is a key risk in our medium-term financial planning. We therefore cannot rely on any future increases in government funding to close our budget gap unless we have had confirmation of it or can reasonably expect it based on experience.

In working to balance the budget, we have worked in a cross-council way to identify the areas for saving or additional income, and the areas where transformation is required to drive efficiencies. Individual services do not have a savings target, and it is the responsibility of senior leaders to identify together the best ways to balance the budget across the whole council. We prioritise the resources available to us to meet the changing and growing needs of communities, and only consider service reductions as a last resort.

Services should review their budgets each year to identify any areas that have been given budget in excess of that needed to deliver the service. This is particularly the case in demand-led budgets, where estimates of growth or demand patterns will have been used and may subsequently change. In undertaking this review, services should bear in mind the corporate reserves position and the general provision for risk, and not assume an excessive amount of risk or contingency needing to be met within service budgets.

The Council also undertakes an annual budget review and rebaselining during the first quarter of each financial year to reassess the budget position in light of developments from the point at which the business plan is approved by Full Council in the preceding February. This allows the budget to be flexed to take account of material changes in circumstances such as significant increase in inflationary pressures or any new legislative requirements. This can contribute towards closing the budget gap in future years if budgets are reduced.

If savings are identified and made in the current financial year but were not planned for, for example a reduction in cost on a new contract, then these will be factored into the business plan for the next financial year. In the meantime, they can be used to mitigate other pressures or funding can be transferred to the general reserve, but they should not be reinvested into ongoing costs.

In generating additional income, we will ensure the Fees & Charges policy is reviewed annually and should assume that by default, charges should go up by inflation each year if permitted.

As well as considering further savings or generating additional income, we need to ensure our projections for income from taxation are accurate. We will work with District Council colleagues, who collect local taxation on our behalf, at several stages throughout the year to receive updated projections for tax base levels and collection rates. Strategy & Resources Committee will also consider an updated approach to the level of Council Tax

Section 9 - Reserves Policy & Position

We need reserves to protect and enhance our medium-term financial sustainability. In particular, reserves are necessary to:

- maintain a degree of in-year financial flexibility
- enable us to deal with unforeseen circumstances and incidents
- set aside monies to fund major developments in future years
- enable us to invest to transform and improve service effectiveness and efficiency
- set aside sums for known and predicted liabilities
- enable us to deal with any unexpected changes in legislation or court judgements
- provide operational contingency at service level
- provide operational contingency at school level

We must also bear in mind the risks and sensitivity of assumptions outlined in chapter 9 above.

Reserve types

The Council maintained the following types of reserve coming in to 2021/22:

- **General reserve** – a working balance to cushion the impact of uneven cash flows. The reserve also acts as a contingency that we can use in-year if there are unexpected emergencies, unforeseen spending or uncertain developments and pressures where the exact timing and value is not yet known and/or in the Council's control. The reserve also provides coverage for grant and income risk.

- **Earmarked reserves** – reserves we have set aside to meet known or predicted liabilities (such as insurance claims), or that we set aside for specific and designated purposes (such as a reserve for risks within adult social care).

- **Schools reserves** – we encourage schools to hold general contingency reserves within advisory limits. The Chief Finance Officer and Director of Education, in collaboration with Schools Forum, monitor schools above the advisory limits, and take steps to encourage appropriate deployment. However, the Council's powers to intervene and insist on spending within delegated and ring-fenced schools budget is limited by legislation. It is also notable that after taking account of the carried forward deficit on the High Needs Block of the Dedicated Schools Grant, the consolidated schools balance is now negative. The Council is taking steps to manage demand on the high needs block and lobby government for a more sustainable long term funding solution.

- **COVID-19 related** – the Council received additional one-off funding from government related to the pandemic in advance of spending requirements. We earmarked some of that funding t to offset the medium- and longer-term effects of the pandemic and recovery.

- **Transformation Fund** – a reserve created several years ago from funding generated by a revision to the Council's policy on minimum revenue provision. It has a set of principles used to access funding and was designed to enable investments that deliver ongoing financial returns.

In considering the planning for 2022-27, we are mindful of the great deal of additional uncertainty that we face, particularly from:

- The long-term effects of COVID-19, and the costs we might face as we recover from the pandemic, bearing in mind the earmarked reserve for COVID-19 costs that we have
- The growing deficit on the High Needs Block of the Dedicated Schools Grant, which is projected to be around £37m at the start of 2022/23
- Announced government reforms, particularly in adult social care funding, where we do not yet have full details
- The ongoing effects of the United Kingdom's exit from the European Union
- Potential, unpredictable disruptions to global supply chains, increasing prices or causing shortages of goods
- Climate change and the need to move towards being a net-zero county

We also need to consider the general economic conditions, the certainty of these conditions, and the probability and financial impact of service and business risks specific to the Council in order to calculate the level of reserves we need to hold.

At the same time, we do need to ensure there are sufficient reserves to enable the funding of one-off costs that enable innovative or transformative pieces of work to take place, particularly where they contribute towards the longer-term financial sustainability of the Council.

We therefore need to review:

- The adequacy of the general reserve
- Providing an offset for the High Needs Block deficit
- Funds held for one off investment
- How we use our COVID-19 reserve

Adequacy of the general reserve

In previous years, the Council has set the general reserve at 3% of gross non-school expenditure. This was reviewed ahead of setting the 2021/22 budget within the context of considerably increased uncertainty resulting from the COVID-19 pandemic and was deemed to be still appropriate given the additional contingency planning that had been part of core service budgeting process.

As a result of the increasing uncertainty in the medium-term set out above, that target for the underlying balance should be increased to be no less than 4% of gross non-school spending for 2022/23 and maintained at that level through the whole MTFS period. The increase reflects a strategy of managing risks to the Council corporately rather than in specific services, reducing the level of ongoing budget that is committed to contingencies in services.

If any of the general reserve is required to be used in a given year to meet a revenue pressure, it will be topped-up as a matter of course in the subsequent business planning round.

If the general reserve is above its targeted level at the end of a financial year, we will retain at least as much as is needed to keep the fund at the projected 4% required in the fifth year of the MTFS. Any further balance may be retained in the general fund or may be transferred to top-up any other reserve as required

The table below sets out some of the known risks presenting themselves to the Council and their indicative values. There will inevitably be other, unidentified, risks and we have made a limited provision for these as well.

We consider this level to be sufficient based on the following factors:

- The Council continues to hold substantial rolled-forward COVID-19 grant funding, which can be used in a sustainable way to offset COVID-19-related pressures
- We retain substantial other reserves that, while earmarked, are not necessarily committed to expenditure

Table 9.1: Target general reserve balance for 2021-22 to 2025-26

Risk	Source of risk	Value £m
Inflation	0.5% variation on Council inflation forecasts.	1.1
Demand	4% variation on Council demand forecasts.	8

Interest rate change	0.5% variation in the Bank of England Base Rate.	0.2
Council Tax	Inaccuracy in District tax base forecasts and collection levels.	2
Business Rates	Inaccuracy in District tax base forecasts of County share of Business Rates to the value which triggers the Safety Net.	1
Business Rates payable	Impact of revaluation on Business Rates payable.	0.5
Unconfirmed specific grant allocations	Value of (as yet unannounced) specific grants different to budgeted figures.	1.5
Deliverability of savings against forecast timescales	Risk to contract savings due to financial challenges faced by suppliers, increase in service user need due to the pandemic, shortfall in commercial income due to economic downturn	5
Non-compliance with regulatory standards	E.g. Information Commissioner fines.	0.5
Major contract risk	E.g., contractor viability, misspecification, non-delivery.	3.2
Unidentified risks	Unknown	2.7
Balance		**25.7**

High Needs Block Deficit

The deficit on the High Needs Block is estimated to be around £38m at the start of 2022/23. This is partly offset by balances held by maintained schools but is still in overall deficit. This deficit is currently ring-fenced to the DSG, and we are not currently required to use general reserves to offset it. Many Councils now have deficits on the High Needs Block, so it is a national issue.

The statutory instrument on treatment of this deficit expires at the end of 2022/23, and it is not clear how we will be expected to manage this deficit thereafter. We are working to reduce the growth in the deficit year-on-year through a programme of transformation, but realistically we are unlikely to be able to mitigate the whole deficit through this route.

There is a risk that government requires councils to meet their High Needs Block deficits. Although that is considered a worst-case outcome, if that were to happen, it could potentially overwhelm our general reserve provision causing significant medium-term disruption to our financial planning. Given the scale of the risk, it would be prudent to earmark some reserves to mitigate this threat. Bearing in mind the national scale of the issue, the transformation programme to reduce deficit growth, reserve balances held by schools, and ongoing engagement by the Department for Education with councils, we intend to earmark funding to offset this year's expected growth in this deficit. We would call this the High Needs Block Offset.

The Council cannot drain its general reserve to create this offset reserve, and so it would need to be through a reallocation of other existing reserves.

Investment

It remains a priority of the MTFS to ensure there is sufficient one-off resource to fund proposals that help us transition to a more sustainable future. That may be increased financial sustainability, environmental sustainability, or better and more sustainable outcomes for service-users.

[We will announce further details of this investment approach alongside our strategic framework and budget proposals at the January Strategy & Resources Committee]

Deployment of COVID-19 reserve

During 2020/21 and early 2021/22, central government provided significant support to Councils dealing with the effects of the COVID-19 pandemic in the form of un-ringfenced grant funding.

We faced substantial increases in costs during the pandemic, but several funding sources announced later in 2020/21 reduced the need to use the un-ringfenced grant. The main additional funding sources announced were:

- Support for infection control and testing in social care providers
- Outbreak management funding
- Compensation for lost sales, fees & charges
- Government funding/supply of Personal Protective Equipment

Much of our un-ringfenced funding was anticipated to have been used to meet costs that were later covered by the above funding. As a result, we retain a reserve created by this grant, which is available to use to mitigate the ongoing effects of COVID-19.

We expect to be feeling the effects of COVID-19 on our service delivery and financial position for at least several more years. This will particularly be felt in parts of our adult social care demand, uplift requirements for adult social care contracts, and lost income in some services. We will therefore release part of this grant reserve into revenue in a sustainable, reducing profile over the medium term.

This will be used to fund specific pressure lines that remain in in the business plan around the effects of COVID-19 on demand and income, as well as funding part of the Adult Social Care demand growth that we believe is the result of the ongoing effects of the pandemic on people's needs.

Table 9.2: Estimated reserves balances over 2022-27

Balance as at:	31 March 2023 £m	31 March 2024 £m	31 March 2025 £m	31 March 2026 £m	31 March 2027 £m
General reserve	25.7	26.3	26.8	27.2	27.2
Other earmarked reserves	132.8	122.8	113.4	105.8	99.1
Total	**158.5**	**149.1**	**140.2**	**133.0**	**126.3**
General reserve as % of gross non-school budget	4.0%	4.0%	4.0%	4.0%	4.0%

Section 10 - Risks & Sensitivity

In providing budget estimates, we have carefully considered financial and operational risks. The key areas of risk, and the basic response to these risks, are as follows:

- **Containing inflation to funded levels** – we will achieve this by closely managing budgets and contracts and further improving our control of the supply chain.
- **Managing service demand to funded levels** – we will achieve this through clearer modelling of service demand patterns using numerous datasets that are available to our internal Research Team and supplemented with service knowledge. A number of the proposals in the Business Plan are predicated on averting or suppressing the demand for services.
- **Delivering savings to planned levels** – we will achieve this through SMART (specific, measurable, achievable, relevant and timely) action plans and detailed review. All savings – efficiencies or service reductions – need to be recurrent. We have built savings requirements into the base budget, and we monitor these monthly as part of budgetary control.
- **Containing the revenue consequences of capital schemes to planned levels** – capital investments sometimes have revenue implications, either operational or capital financing costs. We will manage these by ensuring capital projects do not start without a tested and approved business case, incorporating the cost of the whole life cycle.
- **Responding to the uncertainties of the UKs exit from the European Union** – we have fully reviewed our financial strategy in light of the most recent economic forecasts and continue to develop plans in response to emerging risks and opportunities presented as a result of Brexit.
- **Future funding changes** – our plans have been developed against the backcloth of continued uncertainty due to delays in the introduction of significant reforms to Local Government funding.
- **Managing future carbon liabilities** – the Council has committed to deliver net-zero carbon emissions by 2050 as part of its pledge to tackle the climate emergency. There is a risk that additional financial resources may be required to achieve this aim which have not been fully accounted for within the MTFS. The funding allocated to deliver the Climate Change and Environment Strategy will be reviewed annually in light of progress towards achieving the Council's net-zero carbon commitment.
- **Responding to social care reforms** – we will estimate the cost of these reforms and make budget provision for them when we are able to. We will work closely with NHS partners to ensure that additional funding provided to the health and social care system locally is appropriately used to meet the cost of government reforms.

In addition to these risks, there remains a general risk around recovery from the pandemic and the speed of economic recovery, as well as the prospects for the economy over the medium term. This may increase costs the Council faces, increase demand for our services, and reduce income (through lower charging income or taxation relief).

There is also a risk of sensitivity in all of the assumptions made throughout this strategy. The level of sensitivity of key assumptions is shown in the following table:

Table 11.1 – sensitivity analysis

10% savings delivery variance	+/- £2.3m
+/- 1% pay inflation	+/- £1.3m
+/- 1% general inflation	+/- £1.0m
+/- 1% Council Tax base	+/- £3.2m
+/- 1% Council Tax collection rate	+/- £3.2m
+/- 1% Business Rates base	+/- £0.7m
+/- 1% income from sales, fees & charges	+/- £1.3m
+/- 5% on cost of borrowing	+/- £1.0m
Range of sensitivity	**+/- £14.0m**

Uncertainties remain throughout the planning period in relation to the above risks. In line with good practice, we intend to reserve funds that we can use throughout and beyond the planning period. This is set out in section 9 above. Together with a better understanding of risk and the emerging costs of future development proposals, this will help us to meet such pressures.

Section 12 - Business Plan roles and responsibilities

The Business Plan is developed through the Council's committee structure. It is therefore beneficial to clarify the respective roles and responsibilities of committees within this process. These are defined in the Constitution but are set out below in order.

Full Council

Council is the only body that can agree the Council's budget and the associated Council Tax to support the delivery of that budget. It discharges this responsibility by agreeing the Business Plan in February each year. In agreeing the Business Plan the Council formally agrees the budget allocations for the service blocks (currently based on a departmental structure). The Business Plan includes both revenue and capital proposals and needs to be a 'balanced' budget. The following is set out within Part 3 of the Constitution – Responsibility for Functions.

Council is responsible for:

"(b) Approving or adopting the Policy Framework and the Budget

(c) Subject to the urgency procedure contained in the Access to Information Procedure Rules in Part 4 of this Constitution, making decisions about any matter in the discharge of a committee function which is covered by the Policy Framework or the Budget where the decision-making body is minded to make it in a manner which would be contrary to the Policy Framework or contrary to, or not wholly in accordance with, the Budget

(d) Approving changes to any plan or strategy which form part of the Council's Policy Framework, unless:

  i. that change is required by the Secretary of State or any Government Minister where the plan or strategy has been submitted to him for approval, or

  ii. Full Council specifically delegated authority in relation to these functions when it approved or adopted the plan or strategy"

Strategy & Resources (S&R) Committee

S&R has the responsibility for the delivery of the Business Plan as agreed by Council. It discharges this responsibility through the service committees. In order to ensure that the budget proposals that are agreed by service committees have an opportunity to be considered in detail outside of the Council Chamber, those proposals will be co-ordinated through S&R, though Full Council remains responsible for setting a budget. S&R does not have the delegated authority to agree any changes to the budget allocations agreed by Council save for any virement delegations that are set out in the Constitution.

The following is set out within Part 3 of the Constitution – Responsibility for Functions.

> “The Strategy and Resources Committee is authorised by Full Council to co-ordinate the development to Full Council of the Strategic, Policy and Budget Framework, as described in Article 4 of the Constitution, including in-year adjustments.”
>
> “Authority to lead the development of the Council’s draft Business Plan (budget), to consider responses to consultation on it, and inform the draft Business Plan to be submitted for approval by Full Council.”
>
> “Authority for monitoring and reviewing the overall performance of the Council against its Business Plan.”
>
> “Authority for monitoring and ensuring that Policy and Service Committees operate within the policy direction of the County Council and making any appropriate recommendations.”

S&R is also a service committee in its own right and, therefore, also has to act as a service committee in considering proposals on how it is to utilise the budget allocation given to it for the delivery of services within its responsibility.

Service Committees

Service committees have the responsibility for the operational delivery of the Business Plan as agreed by Council within the financial resources allocated for that purpose by Council. The specific functions covered by the committee are set out in the Constitution but the generic responsibility that falls to all is set out below:

> “This committee has delegated authority to exercise all the Council’s functions, save those reserved to Full Council, relating to the delivery, by or on behalf of, the County Council, of services relating to…”