Cabinet

8 July 2021

A Financial Framework for the 2022/23 MTFS Refresh

Recommendations

That Cabinet:

1) Note the emerging financial position within which the 2022/23 budget and 2022-27 Medium Term Financial Strategy will be developed;

2) Agree the proposals for the refresh of the 2022/23 MTFS and Capital Strategy, as set out in Sections 3 and 4;

3) Note the requirement for the Authority to set a sustainable balanced budget which shows how income will equal spend over the short- and medium-term; and

4) Approve the timetable for agreeing the 2022/23 budget.

1. Purpose of the Report

1.1. Over the five years to 2025/26 the MTFS approved in February 2021 was balanced, considering likely additional spending need and the expected level of resources. It required the delivery of £48.2m of savings and the use of £32.9m of reserves.

1.2. The 2022/23 MTFS refresh therefore has a strong and robust starting point. It will update the figures for additional spending need and the resource forecasts based on the latest information available and reflect how the current year's (2021/22) financial position looks compared to the planned budget. It will also extend the MTFS into 2026/27 so the commitment to having a balanced five-year rolling MTFS is maintained.

1.3. The context in which the 2022/23 refresh is happening continues to be dominated by Covid. Added to this are significant uncertainties around Government policy in terms of the Comprehensive Spending Review, the

Local Government Finance Settlement and funding reforms, potentially major reforms with Green papers on Social Care and White Papers on Devolution and possible Planning reform and the roll out of the Government's proposals around levelling up and the UK Shared Prosperity Fund.

1.4. The economic situation remains hugely challenging, and we continue to be faced with rising demand for services as well as inflationary pressures as a result of supply/labour shortages. The direct and indirect impacts of all these factors on the County Council as well as our partners are both unknown and highly volatile at this stage.

1.5. The purpose of this report is to bring these strands together and to provide a framework for Cabinet to consider. The recommended approach will enable the Council to respond effectively to changing circumstances while maintaining a longer-term focus on the Council's financial sustainability. The report then goes on to set out the key points and proposed timetable of key dates between now and the budget setting Council meeting in early February 2022.

2. Framework for a Robust, Sustainable and Financially Resilient Warwickshire

2.1. The strength of the Authority's balance sheet has traditionally meant we have been in a position to develop the future year's budget and MTFS as a largely standalone exercise with only material demand pressures arising through budget monitoring impacting on planning for future years. The uncertainty and financial commitment created by Covid-19, the potential latent demand in the system and the investment in WPDG and WRIF means this is no longer the case.

2.2. Instead the different dimensions need to be considered together to ensure the County Council remains a robust, sustainable, and financially resilient Authority. Each of the dimensions will have a different purpose and provide different intelligence to ensure we have a resourced and deliverable Council Plan:

- Further review of the 2020/21 outturn, reported to Cabinet in June will:
  - Determine the extent to which the Authority's reserves can be used to support the MTFS either through funding investment or smoothing the delivery of savings ; and
  - Identify any further requirement to, or opportunities for, right-sizing.

- The forecast 2021/22 outturn position and rephased capital programme will determine the level of resources required in 2021/22 compared to the approved budget, the resourcing of investment in response to the on-going impact of Covid-19, and revised levels of funding now available; and

- The 2022/23 MTFS refresh will:
  - Determine the likely levels of resources and balance sheet capacity available over the medium term;
  - Determine the level of spending priority commitments arising from the Authority's ambitions over the medium term;
  - Determine the impact on the Authority's balance sheet and cash resources; and
  - Given that there is likely to be a gap, identify additional options to deliver budget reductions that can be evaluated alongside spending priorities.

2.3. This will result in a range of activity, information and intelligence gathering and reports that will need to be brought together before decisions are made over the next six months. The overall objective is to ensure a transparent approach, taking into account the full risks and implications for services and communities, to meet the overarching aim of being a robust, sustainable and financially resilient Authority well-placed to rise to the challenge of meeting the ambitions set out in the refreshed Council Plan in a post-Covid environment.

2.4. More detail on the proposed activities and how they will contribute to meeting our financial aims is set out in Section 3.

3. 2022/23 MTFS Refresh

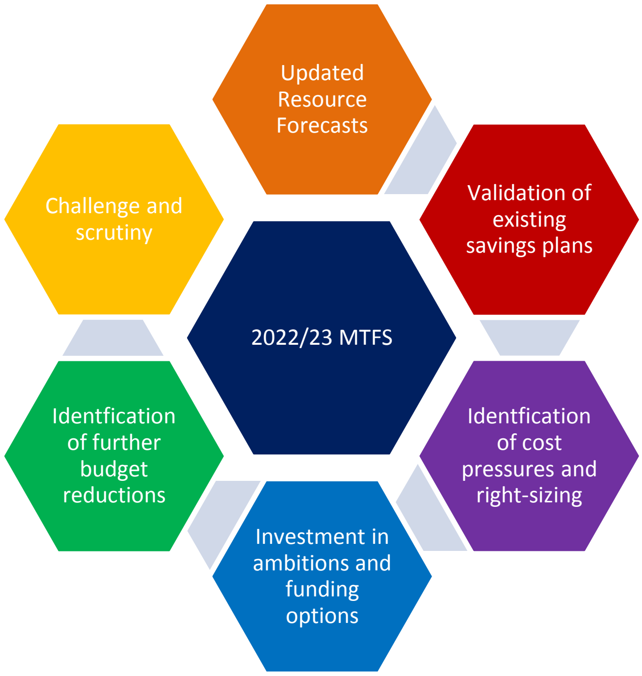
3.1. The starting assumption for the 2022/23 MTFS refresh is that the impact of Covid-19 in 2021/22 can be manged in year through robust budget management from within the additional resources provided by the Government/NHS. If this proves not to be the case, then the approach set out in the report and the rigour with which it is pursued becomes even more important.

3.2. The approach set out in the report is a holistic one which combines the uncertainty over our medium-term resource levels, growing demand and cost pressures and the effect of the use of our balance sheet to invest in Warwickshire Property and Development Group (WPDG and Warwickshire Recovery and Investment Fund (WRIF). The delivery of the refreshed Council

Plan will require the impact of any proposals on both the MTFS and our balance sheet to be considered together. This, combined with the uncertainty over our medium-term resource levels, means the 2022/23 MTFS refresh will be more complex than usual. It is likely to provide Members, with some difficult choices about priorities and the level of assurance around the potential significance and volatility of our assumptions requiring scenario planning and sensitivity analysis.

3.3. Diagram 1 shows the areas of activity that will need to be undertaken to deliver a refreshed 2022/23 MTFS, alongside a further review of reserves.

Diagram 1: Areas of Activity to Deliver a Refreshed MTFS



3.4. Updated Resource Forecasts

The basic model of resource forecasting used for the 2021/22 MTFS remains valid. However, the level of uncertainty we continue to face means, at least initially, we will need to plan for a range of potential resource scenarios. We will only be able to narrow these down as the economic position, as we move towards a post-Covid environment and the Government's national approach to recovery becomes clearer.

Table 1 summarises the level of additional savings required from 3 broad scenarios. and **Appendix A** outlines the assumptions that underpin them. The scenarios are broadly based on:

- Best Case – minimal recession, return to previously levels of activity by April 2022

- <u>Most Likely</u> – gradual recovery over the next 18 months through to April 23; and
- <u>Worst Case</u> – medium term recession lasting whole of MTFS period with some minimal recovery from year three onwards.

Table 1: Additional MTFS Savings Required as part of 2022/23 MTFS Refresh			
	Best Case	**Most Likely**	**Worst Case**
New savings in 2022/23	£0m	£1m	£24m
New savings over MTFS (including the figures above)	£0m	£21m	£96m

The five key variables in all the scenarios are the annual growth in the council tax taxbase, inflation and then the three variables over which we have more influence – the DSG deficit, the level of additional spending allocations whether driven by demand or priorities and the annual council tax increase. All assume Members support continuing to increase the council tax by 2% per annum and take the additional 2% adult social care levy increase in 2022/23. A reduction of 1% in the council tax increase in any one year would increase the level of savings required by £3.2m.

These resource assumptions will determine the level of further budget reductions or additional income generation the Authority will need to plan for over the period 2022-27. The 'most likely' scenario is that £21m additional savings will be needed in addition to £48.2m already included in the MTFS approved in February 2021 and the £97.3m delivered since 2014.

The need to make the 'right' savings that support the delivery of the Council Plan and do not stifle recovery, increases the on-going importance of effectively managing the Council's spend. The availability of reserves will be critical to allowing the managed, effective implementation of the necessary changes to services to deliver the savings needed, such as the investment in digital and data to enable the delivery of savings through automation and technology. However, it should be noted that any use of reserves for this purpose impacts potential to increase the investment funds and the resources available to invest in the delivery of the refreshed Council Plan.

3.5. <u>Validation of Existing Savings Plans</u>

Even before the impact of changes to resource forecasts and demand pressures the existing MTFS requires the delivery of £48.2m of savings over five years. It is therefore essential to validate that the plans and savings being targeted are deliverable. The 2022/23 refresh will require detailed action plans for the delivery of planned savings in each of the next two years and outline plans for those for those in the last two years of the current MTFS.

Any reduction in the level of budget reductions delivered, whether as a result of deliverability or acceptability, will increase the level of new savings that need to be identified. The working assumption is that where, as a result of developing robust delivery plans, the existing MTFS savings cannot be delivered alternative deliverable savings will be brought forward for consideration. These alternative savings would be in addition to the savings needed to balance the MTFS.

3.6. Identification of Unavoidable Cost Pressures and Right-Sizing

The approved MTFS includes £5.250m a year for new cost pressures and provision for 2% pay and price inflation each year. This is in addition to the £38.3m (or just over £9.5m a year) for known areas of cost pressure already included within the MTFS.

To place these figures into context, the 2021/22 budget included £20.9m allocations to fund permanent growth in spending need. The MTFS assumes that after the material resetting of budgets in 2021/22 the level of new cost pressures can be reduced by around £5m a year.

The identification of unavoidable cost pressures therefore has two elements – a review of those pressures already indicatively approved in the MTFS and identification of any new pressures that have emerged over the last six months.

A robust, evidence-based approach to both elements will be put in place that will cover the cause of the need for an additional budget allocation, the actions the Service has put in place to manage the cost and the implications for service delivery if the allocation is not supported, as well as a detailed calculation of the expected cost and how the funding will be used. This will be accompanied by any further opportunities for right-sizing identified through in-year budget monitoring.

There are three areas where additional funding has already been identified as potentially being required. These are the same three areas of spending pressure that dominated the 2021/22 refresh:

- One-off funding over five years to offset the forecast overspend on the High Needs DSG over the medium term;
- The continued increase in the cost of placements for Looked After Children both in terms of unit costs and complexity of cases; and
- The increase in demand and cost of provision for children with disabilities.

Funding these pressures alone would outstrip the resources currently available in the MTFS in the next two years. The ‘most likely’ option assumes an additional £3.8m a year will be needed to meet additional cost pressures.

The further key risk here is any potential inflationary/deflationary impact. The economic outlook remains uncertain and each 1% variation in pay and prices compared to the 2% assumed in the MTFS in any financial year will be an additional cost/saving of between £4m and £5m. Currently, the greatest inflationary risks are around labour, given furlough and the lack of supply following the EU exit, and price inflation at least partially linked to the same factors.

3.7. Investment in Ambitions and Funding Options

The 2021/22 MTFS retained the £20m Revenue Investment Funds and an expanded Capital Investment Fund (CIF) to deliver on the ambitions of the Council Plan. The Investment Funds are currently secured as sufficient resource has been set aside as part of the Reserves Strategy for the Revenue Investment Funds and through the provision to meet the cost of servicing the borrowing costs that fund the CIF made in the MTFS.

There is a need to more closely align the use the Investment Funds to proposals emerging from the refreshed Council Plan and in particular the Delivery Plans for the next two years. There is also a need to ensure Funds are available for invest-to-save projects that will deliver material future cost savings/avoidance and hence support the delivery of a balanced MTFS. In particular there is likely to be insufficient resource in the Change Fund that resources operational change across the organisation to meet the level of investment needed for the next phase of digital and data which will be crucial to finding further savings and service improvements.

Therefore, as part of the refreshed MTFS a prioritised pipeline of projects will be developed that can be compared to the level of resources available. Currently, the level of resources available in either the Revenue Investment Funds or CIF is insufficient to meet the ambitions of the organisation or deliver the full pipeline of projects. The options available to expand the resources available to balance the Council’s investment plans to the resources available are:

- To review the Council’s reserves to see if additional resources can be released to top up the Revenue Investment Funds; or
- To take out additional borrowing to fund an increased Capital Investment Fund, with the revenue cost of servicing the borrowing funded through an allocation in the MTFS; and/or
- To limit the schemes from the pipeline that are brought forward for approval to those that are the highest priority compared to the resources available.

3.8. Identification of Further Budget Reductions

The need for additional savings will be identified through an approach that ensures the savings identified are the ’right’ spending reductions for the organisation over the medium term. The proposed approach is:

- Priority is given to investment that delivers budget reductions or cost avoidance in future, with benefits built into the MTFS as part of the decision-making process;
- Services to develop contingency plans that identify how over the medium term the cost of services can be reduced and the investment that would be needed to support this. This should be done within the following hierarchy of options:
    - Invest to save proposals that do not reduce the level of service from automation, innovation, digital and efficiencies;
    - Further right sizing of budgets;
    - Targeted reductions in lower priorities, reflecting benchmarking analysis; and
    - Service reductions.

Alongside this work on identifying budget reductions there will be a further review of reserves to see if we can free some up capacity to allow the lead-in time for transformation and innovation activity to be delivered. This may also need to include choices around the balance of using reserves for investment and the short term off-setting of savings.

3.9. Challenge and Scrutiny

The challenge and scrutiny of proposals will provide the biggest step change to the MTFS process from last year. This includes the changes planned for last year that were delayed due to the impact of Covid. Corporate Board are recommending the introduction of:

- Enhanced scrutiny and assessment of spending/savings proposals brought forward for consideration in much the same way as has been put in place for the investment funds, providing clear recommendations that supports the balancing of priorities;
- The use of evidence, such as benchmarking information, insight into the relationship between cost and performance and learning from innovative developments across the sector, to provide a more robust assurance about current base budgets, and to support the proactive challenge and validation of spending proposals and to provide some strategic insight to potential target savings; and
- Analysing the alignment of spend with the Council Plan objectives and the impact of proposals on performance.

4. Capital Programme

4.1. A new approach to future decisions on capital investment need and the management of the programme was approved alongside the 2020-25 Council Plan and MTFS. The resulting Capital Strategy consisted of three core elements:

- the Capital Strategy;
- the resulting Capital Programme/Pipeline of projects - the content of the capital programme (including schemes to be delivered in 1-3 years); and
- the Capital Framework which demonstrates our compliance with the Prudential Code and sets out the governance and resourcing arrangements needed to deliver and administer the pipeline/programme.

Local authorities are required to approve a Capital Strategy on an annual basis. For 2022/23 the annual refresh will ensure the Strategy is consistent with the priorities and outcomes of the Council Plan and associated Delivery Plans and aligned to the emerging thinking on long term place-shaping. This is consistent with the intention of the Capital Strategy to shift to a 20-30 year line of sight and create a more strategic focus to our approach to capital and investment.

5. The Need for a Balanced Budget

5.1. In putting forward their proposals Members are reminded that local authorities are required by law to have a balanced budget. However, what is meant by 'balanced' is not defined in law. A prudent definition of a sustainable balanced budget is a financial plan based on sound assumptions which shows how income will equal spend over the short- and medium-term i.e. the five years of the rolling MTFS. Therefore, for the purposes of the proposals being developed the medium term has been taken as the five years 2022/23 to 2026/27.

5.2. To avoid an unbalanced budget the Local Authority has to be financially resilient. Setting a clear MTFS helps clarify expected income and expenditure. Awareness of the funding available in the forthcoming years means the Council stands a better chance of balancing the budget. Reserves are a useful option for balancing the budget in the short-term, but they can only be used once. Consequently, proposals will be developed on the basis that reserves should not be used to pay for day-to-day expenditure and that they will be replenished when the short-term need has passed, subject to a risk assessment. This will ensure the MTFS for 2022-27 will be fully balanced on an ongoing basis.

5.3. This is consistent with the Reserves Strategy approved as part of the MTFS in February 2021, with the risk assessments being updated twice a year.

Next Steps

5.4. The starting assumption for the 2022/23 MTFS refresh is that the impact of Covid-19 in 2021/22, in excess of the available Government funding, can be manged in year through robust budget management, including the early tackling of emerging areas of overspend, and the use of reserves. If this proves not to be the case, then the approach set out in the report and the rigour with which it is pursued becomes even more important.

5.5. The approach set out in the report is a holistic one which combines the uncertainty over our medium-term resource levels, growing demand pressures and the resourcing of the delivery of the Council Plan, including the use of our balance sheet. This means the 2022/23 MTFS refresh will be more complex than usual and is likely to require some difficult choices about priorities.

5.6. Following Cabinet's approval of the approach outlined in the report Services will begin work identifying and quantifying any costs pressures, the opportunities for investing in the Council's ambitions and options for future budget reductions and invest-to-save proposals. This work will be aligned to the approach to Integrated Planning and the refresh of the Council Plan set out in a separate report on today's agenda and informed by the considerations of the Conservative Budget Working Group.

5.7. The next reports to Cabinet will be the first 2021/22 Financial Monitoring report in September 2021. This will start to clarify the assumptions made in setting out the forecast resource forecasts that underpin the MTFS.

5.8. The proposed timetable of formal reports through to Council agreeing the 2022/23 budget and MTFS in February 2022 is shown below.

Approach to Agreeing the 2022/23 Budget and 2022-27 MTFS	
Date	**Report**
9 September 2021	• Report to Cabinet on the 2021/22 Quarter 1 Financial Monitoring
11 November 2021	• Report to Cabinet on the 2021/22 Quarter 2 Financial Monitoring
9 December 2021	• Report to Cabinet on the draft 2022/23 budget proposals, MTFS, capital strategy and review of reserves
December and January	• Political Groups continue to work on their budget and MTFS proposals
27 January 2022	• Report to Cabinet outlining final information to be used in setting the budget and the Strategic Director for Resources reserves risk assessment • Report to Cabinet on the 2021/22 Quarter 3 Financial Monitoring

	• Cabinet release the Conservative Group's 2022/23 budget resolution(s)
Late January 2022 to early February 2022	• Opposition Groups release any amendments to the Conservative Group's proposals
8 February 2022	• Council sets 2022/23 budget and council tax, 2022-27 MTFS, the Capital Strategy and the 2022/23 Treasury Management and Investment Strategies

6. Financial Implications

6.1. There are no direct financial implications as a result of this report. The report sets out the proposed approach to ensuring the Authority remains financially resilient and sustainable going forward.

7. Environmental Implications

7.1. The Council Plan engagement will specifically address climate change and environmental issues to inform the final plan and MTFS.

8. Background Papers

8.1. None

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Elected Members have not been consulted in the preparation of this report.

Appendix A

Resource Scenarios and Underlying Assumptions

	Best Case	Most Likely	Worst Case
New savings in 2022/23	£0m	£1m	£24m
New savings over MTFS	£0m	£21m	£96m
Assumptions			
Core BCF/iBCF funding	All social care grants continue for MTFS period with Public Health Grant increase by 2%	All social care grants continue for MTFS period cash flat	1% annual reduction in core government grants
Council Tax Collection Fund Deficit	£2m in 2022/23	£8m in 2022/23, £3m in 2023/24	£15m in 2022/23, £5m in 2023/24
Council tax taxbase	1.5% growth in 2022/23, thereafter 2%	1% growth in 2022/23, thereafter 2%	1% decrease in 2022/23, thereafter 1%
Council tax increase	2% per annum plus 2% adult social care levy in 2022/23	2% per annum plus 2% adult social care levy in 2022/23	2% per annum
Business rates income	Annual 1% growth in taxbase (excluding top-up), deficits met from £8m NNDR appeals reserve, 2% inflationary uplift	Flat taxbase, £8m NNDR appeals reserve used, 2% inflationary uplift	5% reduction in taxbase in 2022/23, flat thereafter, £8m NNDR appeals reserve used, 2% inflationary uplift
High Needs DSG deficit	High Needs DSG brought into balance by end of MTFS period and reserve released MTFS provision remains unchanged in the interim	High Needs DSG deficit provision in MTFS insufficient by £2m, no long-term solution identified	As per current DSG recovery plan £1m annual increase in deficit
Additional permanent spending pressures	Spending pressures met from within the MTFS provision plus £8.5m in 2026/27 to include capital financing costs	Increase provision from £5.250m to £9m a year plus £2.8m in 2026/27 for capital financing	Increase provision from £5.250m to £10m a year plus £2.8m in 2026/27 for capital financing
Price/Income Inflation	Maintained at 2% per annum	Maintained at 2% per annum	Increased to 3% per annum
Pay Inflation	Maintained at 2% per annum	Maintained at 2% per annum	Increased to 3% per annum
Non-delivery of existing savings plan	Current savings plans delivered in full or alternatives identified	Current savings plans delivered in full or alternatives identified	20% non-delivery of current savings and no alternatives identified