COTSWOLD
DISTRICT COUNCIL

Council name	**COTSWOLD DISTRICT COUNCIL**
Name and date of Committee	**CABINET – 17 JULY 2023**
Subject	**2023/24 FINANCIAL PERFORMANCE – HIGH-RISK BUDGETS**
Wards affected	All
Accountable member	Cllr Mike Evemy, Deputy Leader and Cabinet Member for Finance Email: mike.evemy@cotswold.gov.uk
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Summary/Purpose	This report provides members with an initial view on the financial challenge for the Council in the current financial year
Annexes	N/A
Recommendation(s)	*1. To note the initial view on high-risk budgets/financial performance* *2. Agrees to establish a new earmarked reserve "Treasury Management Risk" as set out in para 5.13 of this report*
Corporate priorities	• Delivering our services to the highest standards
Key Decision	NO
Exempt	NO
Consultees/ Consultation	N/A

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1 BACKGROUND

1.1 This report provides members with an initial view on the financial challenge for the Council in the current financial year. The purpose of this report is highlight to members the significant risks, uncertainties and external economic factors that may influence financial performance in the year. The report does not provide an indication on budget variations or the outturn forecast. This will be provided in the Q1 Financial Performance report in September 2023.

2 EXECUTIVE SUMMARY

2.1 This report sets out the key risks, uncertainties and external economic factors that may have an impact on the Council's finances over the 2023/24 financial year.

2.2 The 2023/24 General Fund revenue budget is supported by £0.860m from the Financial Resilience Reserve. The report identifies a number of external economic factors and high-risk budget areas that may increase pressure on the Council's Financial Resilience Reserve.

2.3 Inflation has remained higher than the Government's target with CPI, RPI and core CPI rates a cause for concern.

2.4 The Bank of England has raised the base rate to 5.00% to tackle inflationary pressure in the economy. This has led to increased mortgage rates which are likely to add pressure to household budgets.

2.5 High-risk budgets have been identified on the basis of prior year financial performance, impact from inflation or income loss. Budgets where savings are yet to be delivered in full (e.g. Publica and Ubico savings targets totalling £0.5m) are a specific risk although the Cabinet Transform Working Group (CTWG) will be considering proposals from service delivery partners in due course. Section 5 of the report provides further detail on these areas.

2.6 The report recommends Cabinet establish a new earmarked reserve "Treasury Management Risk" which will mitigate the risk around future borrowing and potential changes to the accounting treatment on Pooled Funds.

3 INTRODUCTION

3.1 The Council approved the revenue budget and capital programme at their meeting on 15 February 2023.

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3.2 Revenue budget supported by £0.860m from the Financial Resilience reserve with estimates for the year based on board assumptions around expectations for inflation and interest rates.

3.3 The Council has a legal obligation to set a balanced budget each year and to ensure that the budget remains balanced during the financial year. A summary of the General Fund revenue budget is set out in the table below.

Revenue Budget	**2023/24 Original Net Budget (£'000)**
Environmental & Regulatory Services	485
Business Sup. Svcs - Finance, HR, Procurement	1,120
ICT, Change & Customer Services	2,359
Assets, Property & Regeneration	718
Publica Executives and Modernisation	131
Revenues & Housing Support	615
Environmental Services	4,830
Leisure & Communities	1,918
Planning & Strategic Housing	1,947
Democratic Services	1,095
Retained and Corporate	2,277
Subtotal Services	**17,494**
Less: Reversal of accounting adjustments	(1,636)
Revised Subtotal Services	**15,858**
Corporate Income & Expenditure	(1,495)
Provisions and Risk Items	0
Net Budget Requirement	**14,363**
Funded by:	
Council Tax	(6,311)
Retained Business Rates	(4,389)
Government Funding - Grants	(2,905)
Government Funding - NHB	(290)
Collection Fund (surplus) / Deficit	393
TOTAL Funding	**(13,503)**
Budget shortfall/(surplus)	**861**

3.4 This report provides members with a high-level overview of the service budgets considered to be ‘high-risk’ (define) and the wider external economic environment. Important for members to understand how these may impact on the Council’s finances in 2023/24 and influence the approach to the budget setting process/MTFS update that will be considered by Cabinet in the Autumn.

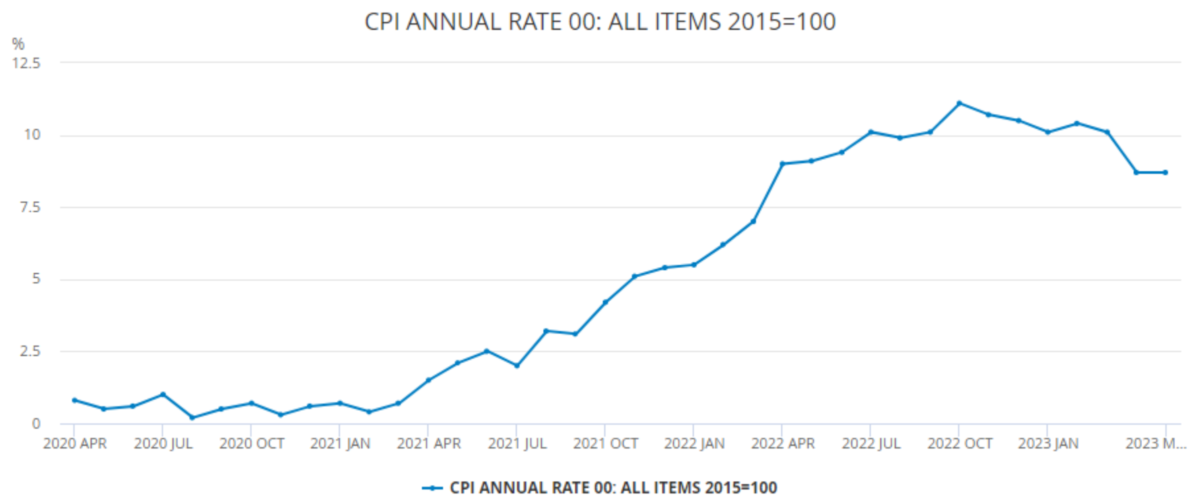
3.5 Q1 Financial Performance report to Cabinet in September will include a detailed budget monitoring position and forecast for the financial year.

4 EXTERNAL ECONOMIC ENVIRONMENT

4.1 As reported to members over the previous financial year, there are a number of external economic factors that will have an impact on the Council's financial performance over the current financial year.

Inflationary Pressures

4.2 The level of inflation, as measured by the Consumer Prices Index, for May 2023 is 8.7% (no change from April, down from 10.1% in March). Although it is not the Government's preferred measure of inflation, the Retail Prices Index is 11.3% (down from 11.4% in April, 13.5% in March). Core inflation (as defined by the Office for National Statistics as the CPI Rate excluding energy, food, alcohol and tobacco) increased to 7.1% in April (up from 6.8% in April, 6.2% in March). It is this measure that is concerning the Bank of England and has led to further increases in interest rates.



4.3 Although general inflation has reduced since the start of the calendar year, the Council is subject to specific inflationary pressures on its services (e.g. fuel costs on waste and recycling service) which have tended to track higher than CPI and RPI.

4.4 The Council will need to take into account the inflationary pressures when monitoring financial performance during the year.

Inflationary Pressures – Pay Award

4.5 With inflation remaining relatively high and not reducing as quickly as anticipated, this may lead to higher wage demands for both private and public sector workers.

4.6 The assumption made for the 2023/24 budget was for an average Pay Award of 4% across Publica, Ubico and Retained staff. Inflationary provision of £1.2m has been included in the budget for the pay award across Publica and Ubico contracts and for retained staff costs.

4.7 Local Government Employers made a final offer to the unions of a £1,925 per FTE employee pay award and if this had been accepted this would have given rise to an increase of between 6% and 7% on staffing costs across Publica and Ubico contracts.

4.8 The unions have rejected this offer and are seeking a pay increase of RPI Inflation plus 2% at every spinal column point. The impact of such an increase across all services would be in the region of £0.7m over and above the budgeted provision.

4.9 At the time of writing this report it is unclear when the pay award will be settled and at what level. The unions are currently balloting members on strike action.

Energy Costs

4.10 The 2023/24 budget and MTFS recognised the significant increase in Energy prices experienced during the previous financial year. Government support for businesses through the energy price cap ended in March 2023.

4.11 Wholesale gas and electricity prices have reduced significantly from the historically high levels experienced during 2022. However, the market is still subject to significant volatility and prices are still more than double what they were at the beginning of 2021. Retail prices remain well above the pre-2021 average meaning the Council will continue to pay much more for energy than it did prior to 2021/22. At this stage it is too early to assess whether the additional amounts included in the budget are adequate. The Council is investing in measures provide green energy (Solar PV) and to reduce its energy consumption over the medium-term.

Interest Rates

4.12 The Bank of England has increased interest rates 13 times since December 2021 in an effort to mitigate inflationary pressures with the latest increase of 0.50% taking the base rate to 5.00% on 22 June 2023. The council's treasury management advisors have forecast further

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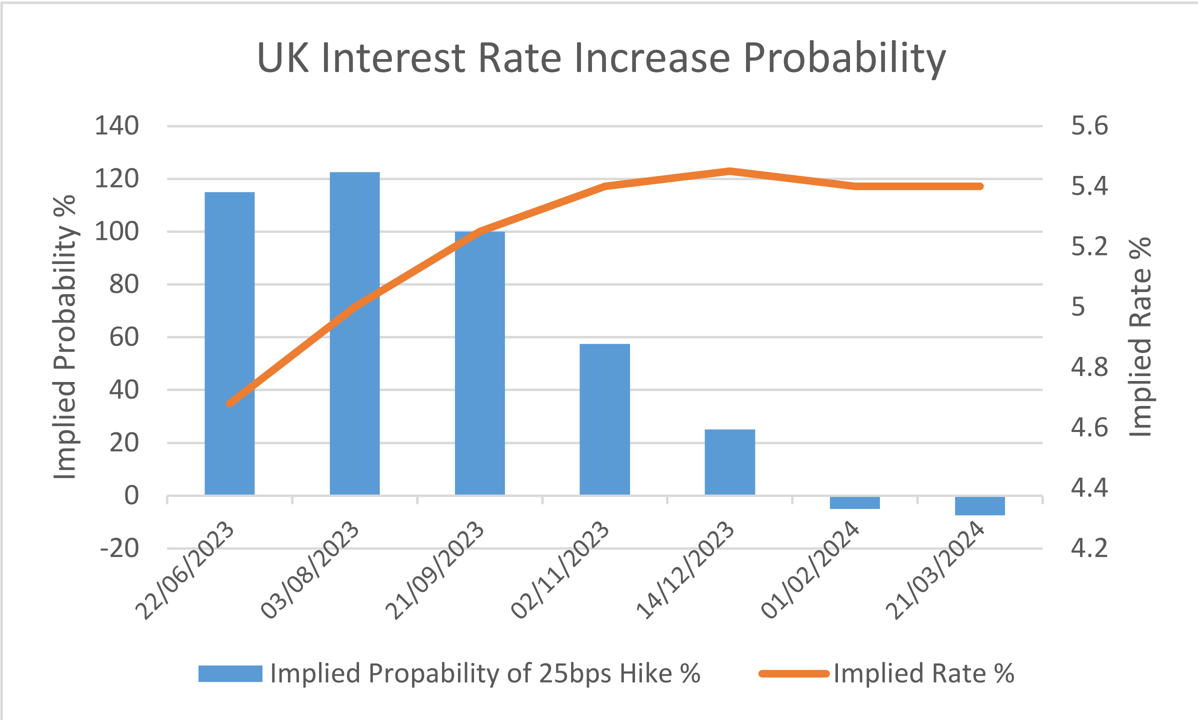
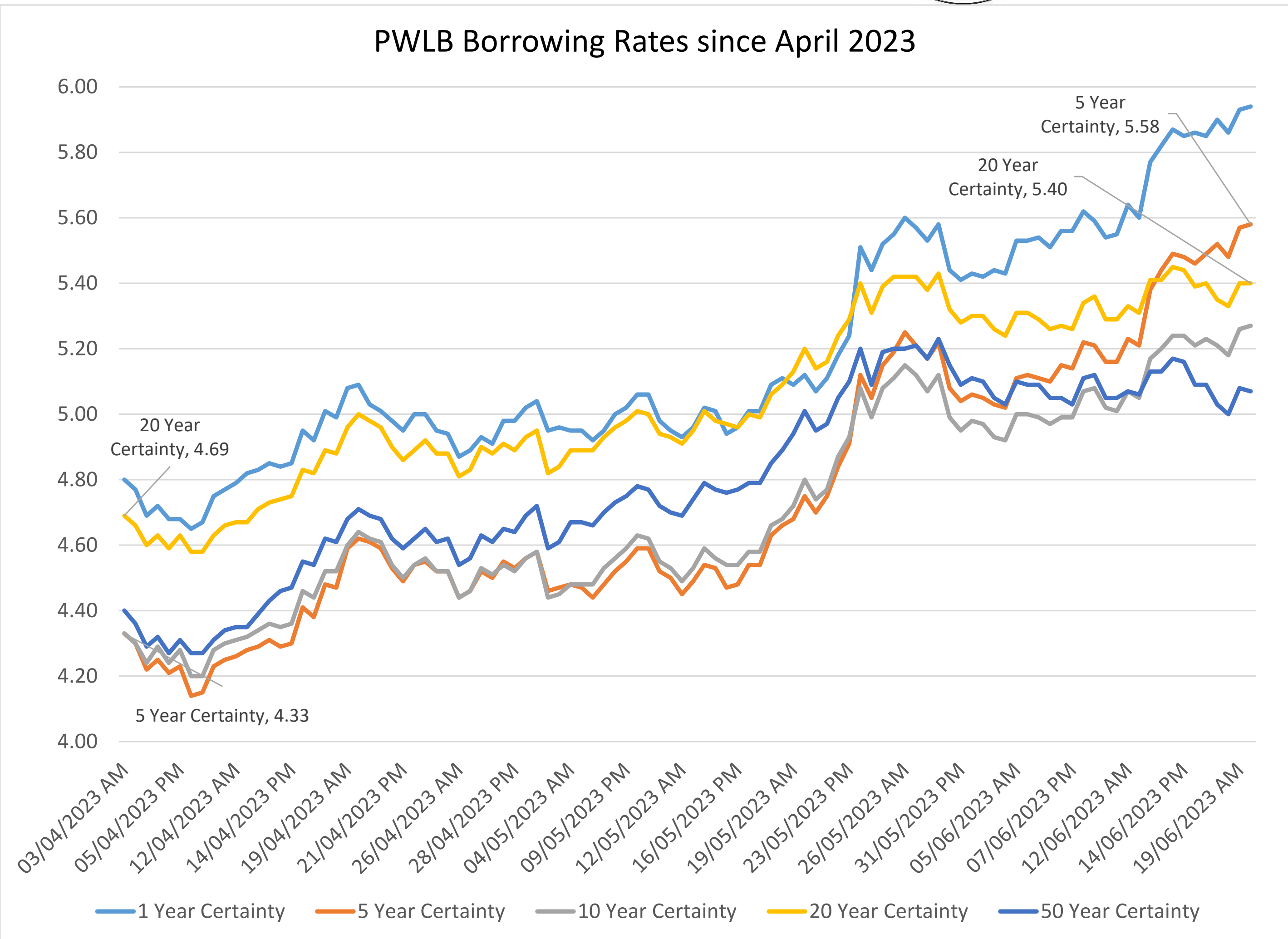
increases during the year with an expectation that the base rate may peak at 5.25% to 5.75%. The graph below is derived from Arlingclose's analysis of the probability of further interest rate increases which was prepared before the recent decision to raise rates on 22 June 2023.



4.13 In order to support the Capital Programme, the Council will need to undertake borrowing during the current financial year although this is dependent on a number of factors. Clearly, with interest rates already, this will impact the expenditure required to service the debt. At the time of writing, PWLB rates have been increasing steadily over the first quarter of the financial year in response to implied Bank Base Rate increases.



4.14 The Council has limited and reducing internal resources to support the capital programme (capital receipts, earmarked reserves). This is not unique to Cotswold District Council with reports in specialist press (e.g. Public Finance) of Councils shelving or scrapping planned capital projects as others costs continue to rise and/or the need to find savings to balance the budget.

4.15 With interest rates expected to remain relatively high during the financial year, the Council will need to ensure capital expenditure and capital financing decisions are made 'in the round'. This will ensure that existing and new capital schemes are not considered in isolation and are prioritised against the Council's Corporate Plan and reference to affordability and deliverability.

4.16 An updated Asset Management Strategy is being prepared which will review and assess the Council's assets and bring forward recommendations for the retention or disposal of the Council's land and property holdings linked to the Council's Corporate Plan and Medium-

Term Financial Strategy (MTFS). Asset disposals would generate a capital receipt which could be utilised in place of external borrowing. The Asset Management Strategy will be considered by Cabinet in the Autumn.

4.17 The Council may benefit from increases in investment income due to the higher interest rates, as outlined in paragraphs 5.11 to 5.13 of the report.

Cost of Living impact

4.18 With inflation rates remaining unchanged in May 2023 with Core CPI increasing there is clearly ongoing pressure on household budgets. It is widely expected that the Bank of England will continue to raise interest rates to tackle inflationary pressures.

4.19 There is also concern around the impact on households from recent increases in mortgage interest rates offered by lenders. With the average 2-year fixed mortgage deal now above 6% it is likely that a greater proportion of household income will be allocated to mortgage interest payments. This may also impact the rental market for properties acquired through buy-to-let mortgages which may see disposals or an increase in rent to mitigate high buy-to-let mortgage costs.

4.20 The Government has so far ruled out any direct intervention arguing that this would place further inflationary pressure on the economy. Whilst mortgage rates of 6% could be seen as reflecting the longer-term interest rate (and certainly much lower than the peak of 15% in the 1980s and 1990s), mortgage holders are more leveraged than before (larger mortgages and lower incomes vs. monthly payments).

4.21 These pressures may lead to increased demand for services providing support to vulnerable individuals and communities, and the Council will need to consider how it would respond to the additional financial pressures outlined above in a targeted and effective way with voluntary and third sector partners.

5 FINANCIAL PERFORMANCE

5.1 For the purposes of this report, General Fund revenue budgets have assessed as high risk using the following criteria:

- DPS: Delivery planned savings
- FPPY: Financial performance of service in prior financial years (2022/23 and 2021/22)
- LOI: Impact of loss of income on revenue budget
- INF: Impact of inflationary pressures
- INT: Impact of interest rates (positive and negative impact)

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5.2 General Fund revenue budgets have been assessed against the criteria outlined above with the high-risk budgets set out in the table below.

Budget Area	Risk Assessment	Expenditure Budget (£'000)	Income Budget (£'000)
Ubico Contract: Waste & Recycling, Street Cleaning	FPPY, LOI,	8,275	(2,431)
Car Parks	FPPY, LOI		(3,010)
Public Conveniences	FPPY, LOI		(88)
Development Management	FPPY, LOI		(895)
Building Control	FPPY, LOI		(360)
Commercial Properties	LOI		(658)
Partner Savings Targets (Publica, Ubico)	DPS	(500)	
Treasury Management – Interest Receivable	FPPY, INT		(830)
Treasury Management – Interest Payable	INT	99	

5.3 Although budget monitoring is yet to be completed for the Q1 Financial Performance report, the high-level assessment of the financial risks and performance to the end of June 2023 is summarised below. Members should treat the initial view as an indication of the direction of travel rather than a detailed review of income and expenditure with associated projections for the financial year.

5.4 **Ubico Contract:** As outlined in paragraphs 4.5 to 4.9, there is a financial risk associated with the outcome negotiations on the pay award for 2023/24 and until this is concluded it is difficult to forecast the outturn position with certainty. The reduction in diesel prices will mitigate some of the financial risk around the pay award, with income from fees and charges (Garden Waste, sale of recycling material) and contributions (Recycling Credits) on target. The table below sets out the Gross and Net cost of services provided by Ubico with £8.275m of Gross Expenditure supported by £2.5m from fees, charges and other contributions. Clearly, inflationary pressure through the Pay Award (paragraphs 4.5 to 4.9) will lead to an overspend against the contract sum without any offsetting actions. The additional contract sum required in 2022/23 was £0.6m.

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	Expenditure			Income	
Waste, Recycling, Street Cleaning and Grounds Maintenance Services	Ubico Contract Costs LAB (£'000)	Other Service Costs LAB (£'000)	Gross Service Cost LAB (£'000)	Income LAB (£'000)	Net Service Cost LAB (£'000)
Bulky Household Waste (Non-Ubico Service)	0	57	57	(79)	(22)
GM - Car Parks	63	0	63	0	63
GM - Cemetery, Crematorium and Churchyards	175	0	175	0	175
Garden Waste Collection	1,315	37	1,352	(1,301)	51
Household Waste	1,622	158	1,780	(24)	1,756
Recycling	2,933	310	3,243	(1,106)	2,137
Refuse / Recycling Organic & Food Waste	685	0	685	0	685
Street Cleaning	1,465	38	1,503	0	1,503
GM - Trinity Road, Offices	16	0	16	0	16
Grand Total	**8,275**	**599**	**8,874**	**(2,509)**	**6,365**

5.5 **Car Parks:** Based on weekly income monitoring, car park revenue is 7% above the same period last year (Weeks 1 to 10 up to 11 June 2023). Whilst this is encouraging, the period covers represents around 16% of the annual income from Car Park fees with Q2 performance (July to September) being critical as this accounts for over 30% of the annual income. The 2022/23 outturn on Car Park income was an income shortfall of £0.408m with £0.120m attributable to the income loss at Rissington Road Car Park. A 7% increase y/y, other things being equal, would reduce the income shortfall significantly when compared to 2022/23 although caution should be exercised as car park income will not follow a linear uplift.

5.6 **Public Conveniences:** Cabinet approved increases to the service charges for the Council's Public Conveniences from 01 April 2023. Whilst the budgeted level of income from service charges increased to £88k, the service requires an ongoing subsidy of £0.194m given the cost of maintaining the 15 sites the Council operates. There has been a reduced level of usage since the Covid pandemic with an income shortfall of £32k in 2022/23 and £26k in 2022/23.

5.7 **Development Management:** Overview and Scrutiny Committee and Cabinet considered the Development Management Improvement Programme report at their meetings in June 2023 in response to the Planning Advisory Service (PAS) review. Whilst this report did not provide any information on the financial performance in the current financial year it did outline improvements that have been made to processes and also set out a number of additional pre-application and discretionary fees that have been adopted from April 2023. The report also outlined the investment being made in the IDOX IT system. Clearly, there remains a significant financial risk to the revenue budget and performance on both income and expenditure will be monitored closely.

5.8 **Building Control:** The building control service operates in a competitive market and the Council will need to review performance against income targets during the year. Over the previous two financial years there has been an income shortfall of £78k and £59k.

5.9 **Commercial Properties:** The Council receives rental income from a number of commercial properties with £0.658m of gross income included in the revenue budget. The majority of properties are fully occupied although there is some concern around the level of rental income that will be attained on multi-tenanted properties given historic levels of under-occupancy and difficulty in attracting new tenants.

5.10 **Partner Savings Targets:** The General Fund revenue budget includes a savings target of £0.250m for both Publica and Ubico. Options for the delivery of these savings from each service partner are being considered by the Cabinet Transform Working Group (CTWG) and will be proposed to Cabinet in due course. Clearly, this remains a significant financial risk in the revenue budget.

5.11 **Treasury Management:** As set out in paragraphs 4.12 to 4.14, increases in the Bank of England Base Rate will have both a positive and negative impact on the revenue budget. Investment income from Treasury Management activities is likely to be above the budgeted level for the year with higher interest rates. Performance of the Council's longer-term investments (Pooled Funds, Real Estate Investment Trusts) remains strong. Income and capital performance of the investments is monitored and benchmarked with strategic advice provided by the Council's Treasury Management advisors, Arlingclose, on investment and borrowing activities.

5.12 Performance and benchmarking information is provided by Arlingclose around 3-4 weeks after the end of the quarter and will be included in the Q1 Financial Performance report to Cabinet and to members of Audit and Governance Committee through the regular Treasury Management reports.

5.13 With the expectation of improved investment returns during the financial year, it is recommended that any additional investment income above the budgeted level is transferred to a new earmarked reserve ("Treasury Management Risk") to manage higher borrowing costs in the short-term and to mitigate potential changes to the accounting treatment of gains and losses on pooled funds from March 2025.

6 CONCLUSIONS

6.1 This report sets out the initial view of the Council's revenue budget position for 2023/24 and an assessment of the potential impact on the Council's finances from the wider economic environment. The detailed Q1 Financial Performance report will be considered by Cabinet at their meeting in September and will provide the budget monitoring position and outturn forecast for the year.

6.2 Issues outlined in this report will also need to be considered as part of the 2024/25 Budget Strategy and update of the Medium Term Financial Strategy.

6.3 The Cabinet Transform Working Group (CTWG) will need to consider the financial risks and uncertainties set out in this report. Specifically, the group will need to understand the financial impact of partner savings proposals and whether they will help the Council to maintain a balanced budget for the year.

7 FINANCIAL IMPLICATIONS

7.1 The financial implications are set out in Section 5 of this report.

8 LEGAL IMPLICATIONS

8.1 None other those identified in 3.3 of the report

9 CLIMATE AND ECOLOGICAL EMERGENCIES IMPLICATIONS

9.1 None

10 ALTERNATIVE OPTIONS

10.1 None

(END)