AGENDA

CABINET

MONDAY, 7 AUGUST 2006

11.00 AM

COUNCIL CHAMBER, COUNCIL OFFICES, ST PETERS HILL, GRANTHAM

Duncan Kerr, Chief Executive

CABINET MEMBERS:	Councillor Mrs. Linda Neal (Leader/ Portfolio: Strategic Partnerships & Community Safety), Councillor Ray Auger (Portfolio: Healthy Environment), Councillor Terl Bryant (Portfolio: Resources & Assets), Councillor Paul Carpenter (Deputy Leader & Portfolio: Access and Engagement), Councillor Mrs Frances Cartwright (Portfolio: Organisational Development & Housing) and Councillor John Smith (Portfolio: Economic Development)
Cabinet Support Officer:	Jo Toomey 01476 406152 e-mail: j.toomey@southkesteven.gov.uk

Members of the public are entitled to attend the meeting of the Cabinet at which key decisions will be taken on the issues listed on the following page. Key decisions are marked *.

1. *MEDIUM TERM FINANCIAL STRATEGY
Report by the Corporate Head of Finance and Resources. (Enclosure)

REPORT TO CABINET

REPORT OF: Corporate Head of Finance and Resources

REPORT NO. CHFR14

DATE: 7th August 2006

TITLE:	Medium Term Financial Strategy 2006/7 to 2011/12 and Budget Preparation
FORWARD PLAN ITEM:	Yes
DATE WHEN FIRST APPEARED IN FORWARD PLAN:	14th April 2006
KEY DECISION OR POLICY FRAMEWORK PROPOSAL:	Budgetary Framework Proposal
COUNCIL AIMS/PORTFOLIO HOLDER NAME AND DESIGNATION:	Resources Cllr T Bryant
CORPORATE PRIORITY:	Effective Use of Resources - Priority A
CRIME AND DISORDER IMPLICATIONS:	None
FREEDOM OF INFORMATION ACT IMPLICATIONS:	This report is available via the Local Democracy link on the Council's website www.southkesteven.gov.uk
BACKGROUND PAPERS:	FIN 236 – Update on Financial Issues 2005/6 FIN 239 – Medium Term Financial Strategy and Budget Preparation 2006/7

INTRODUCTION

1. The purpose of this report is to present the draft Medium Term Financial Strategy to Cabinet. Appendix A to this report provides an updated draft strategy covering the period 2006/7 to 2011/12.

RECOMMENDATIONS

2. It is recommended that the Cabinet:
   a) Recommend to Council the approval of the Medium Term Financial Strategy attached at appendix A to Council
   b) Adopt the budget timetable set out at paragraph 8 of this report
   c) Request that the Corporate Head of Finance and Resources, in consultation with the Portfolio holders for Resources and Communications, draw up budget consultation proposals for implementation during the forthcoming budget cycle

BACKGROUND

3. Report CHFR12 submitted to Cabinet on 10th July 2006 identified a number of key issues that would impact on the Council's Medium Term Financial Strategy (MTFS) and on the budget preparation for 2007/8. The report also provided details of an indicative budget requirement. Members were also advised that an updated strategy would be submitted to Cabinet in August following consideration of the key issues by the Cabinet and Strategic Management Team.

DRAFT MEDIUM TERM FINANCIAL STRATEGY (MTFS)

4. The MTFS forms part of the Council's Budgetary and Policy Framework once approved by Council. The strategy will provide the framework for the development of service plans during the autumn as part of budget preparation for 2007/8. Members will note that some areas of the MTFS will be further developed during this period, as work is and will be ongoing to review and develop the following associated strategies:
   a) Treasury Management Strategy
   b) Capital Strategy
   c) Fees and Charges Strategy

5. The strategy will also need to be updated to take account of the confirmation of formula grant allocation for 2007/8, as the Minister provided an indicative allocation when announcing the grant for 2006/7. In addition a ballot of Tenants on Large Scale Voluntary Transfer is due to take place in the late autumn and the strategy will need to reflect the outcome of the ballot.

6. The MTFS identifies 14 fundamental principles, which when applied will enable the Council to effectively use its resources. These principles build on the Strategy points identified in report FIN239.

INDICATIVE BUDGET

7. In keeping with recent years, it is likely that the level of Council Tax increase acceptable to Government will need to be limited to an increase of less than 5% taking account of the current capping regime, therefore set out below is an indicative budget requirement based on a increase at the ceiling of 5% and an assumed 1% growth in tax base in line with assumptions in previous years.

	2006/7	2007/8	2008/9	2009/10	2010/11	2011/12
	£'m	£'m	£'m	£m	£m	£m
Formula grant indicative allocation	9.272	9.626	9.626	9.857	10.093	10.336
Council Tax Collection Fund surplus	0.039	0.000	0.000	0.000	0.000	0.000
SKDC & Special Expenses Budget requirement funded from Council Tax	5.144	5.466	5.795	6.145	6.514	6.907
	14.455	15.092	15.421	16.002	16.607	17.243

8. The budget preparation timetable is proposed as follows:

2007/8 Service Planning and Budget Preparation Timetable	
September	• Approval of Medium Term Financial Strategy • Service Managers briefings on MTFS implications for preparation of service plans and budgets (mid September) • Gateway reviews of progress towards achieving 2006/7 Service Plan outcomes to inform service planning process • Service Managers commence preparation of draft Service Plans following briefings
October	• Service Managers undertake preparation of draft service plans
November	• Initial Gateway review of draft service plans • Collation of draft budget implications arising out of draft service plans (mid November) • Cabinet draft budget consideration
December	• Final gateway review of draft service plans following collation of budget implications • Cabinet draft budget consideration
January	• Budget consultation
February	• Cabinet present budget
March	• Council set Council Tax

COMMENTS OF CORPORATE HEAD OF FINANCE AND RESOURCES

9. My comments are contained within the body of the report.

COMMENTS OF THE MONITORING OFFICER

10. Once approved the revised draft MTFS will form part of the Council's Budget and Policy Framework.

CONTACT OFFICER

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Medium Term Financial Strategy

Medium Term Financial Strategy

Introduction

The ability to deliver, and to continue to deliver South Kesteven District Council's Vision and Corporate Plan in the future is dependent upon having the required resources to do so. Good financial management remains key to the Council.

At its meeting of 10th July 2006 the Cabinet approved the development of a more strategic forward looking approach to budgeting with a more robust three year planning process, demonstrating the direction of resources towards priority services.
This document sets out the medium term financial strategy for South Kesteven District Council for the five year period 2007/8 to 20011/12, and updates and extends the existing strategy for the period 2006/7 to 2010/11.

South Kesteven has managed its financial resources prudently over many years and as a result is well placed to deliver community priorities into the future. Other documents that are currently under review and which should be read in conjunction with this strategy in the future are: the Capital Strategy; the Asset Management Plan; the Treasury Management Strategy, the Fees and Charges Strategy, the Annual Efficiency Statement and the Financial Regulations.

This strategy identifies a number of fundamental principles, which may be summarised as:

- **Principle 1 - The Community Strategy, Corporate Plan and Annual Performance Plan drive the allocation of resources**. All key decisions of the Council should relate back to the approved priorities of the Council. The Council has adopted a four point prioritisation process:
  - Category A – priority areas for stepped improvement
  - Category B – priority areas for incremental improvement
  - Category M – priority areas for maintained performance
  - Category Z – priority areas for managed dis-investment
- **Principle 2 - Manage financial resources to achieve Efficiency and Value For Money, whilst maintaining a balance between quality and cost effectiveness**
- **Principle 3 - Maintain flexibility to respond to a changing local government environment**
- **Principle 4 - Maintain a sustainable Revenue Budget**
- **Principle 5 – Maintain a prudent approach when making estimates of external funding from Government**

- **Principle 6 - Identify and seek opportunities for external funding whilst maintaining prudent estimates of realisable funding**
- **Principle 7 - Manage the Council's Assets, Reserves, Balances and Receipts to optimise financial returns for future investment in the Council's priorities for the benefit of the Community**
- **Principle 8 - Maintain a robust Capital Strategy to support deliverable medium term capital programmes**
- **Principle 9 - Improve Treasury Management performance**
- **Principle 10 - Balance the need to meet local taxation demands with Community aspirations and ability of local taxpayers to meet them**
- **Principle 11 - Maintain a robust Fees and Charges Strategy**
- **Principle 12 - Manage the impact of the introduction of Local Area Agreements**
- **Principle 13 - Deliver the priorities of the Council without exposing the Council to unnecessary risks by targeting the use of resources linked to corporate risk**
- **Principle 14 - Manage the financial viability of the Housing Revenue Account (HRA) and ballot tenants on the preferred option of LSVT to provide the investment required to deliver Tenant aspirations**

Principle 1 – The Community Strategy, Corporate Plan and Annual Performance Plan drive the allocation of resources **(incorporating the former Strategy 2)**

All key decisions of the Council should relate back to the Community Strategy, Corporate Plan and Annual Performance Plan that reflect the approved priorities of the Council. The Council has adopted a four-point prioritisation process as follows:

- Category A – priority areas for stepped improvement
- Category B – priority areas for incremental improvement
- Category M – priority areas for maintained performance
- Category Z – priority areas for managed dis-investment

The Council undertook a consultation process in 2004 to identify priorities this resulted in the setting of Council priorities based on the above categories. The Council has since undertaken an annual review to ensure they remain fit for purpose. The review incorporates a "[1]Gateway Review" process, whereby, progress towards achieving outcomes and the effectiveness of the individual plans are reviewed.

The Council's Capital and Revenue budgets should be allocated taking account of the four-point prioritisation process. The Capital Strategy and service planning templates are being further developed to enable effective allocation of resources according to priorities.

Category A – Priorities for stepped improvement

Category A priorities are those areas identified for "stepped improvement", as a result of responding to a major national or local priorities. The Council's current Category A priorities are:

- Access to services
- Affordable housing
- Anti-social behaviour
- Communications
- Effective use of resources
- Recycling
- Town centre development and Grantham as a sub-regional centre

Category B – Priorities for incremental improvement

Category B priorities are those identified for "incremental improvement". A list of the category B priorities is appended to this Strategy at appendix 1.

Category M – Priorities for maintained performance

Category M priorities are areas of the Council's operation that have been identified to be "maintained" at the current level of performance or to ensure that a statutorily defined level of service is achieved. Category M priorities are summarised at appendix 2.

Category Z – Service areas identified for managed dis-investment

The Council recognises that the resources available to it are finite and that there is a need to prioritise service investment into to those areas that have been identified as either a category A,B or M. To enable this to be achieved the Council has identified service areas for a managed dis-investment, with a policy to re-invest these

[1] Gateway review involves the service manager, Cabinet Members, members of the Management Board, and Scrutiny Panel members

savings into the priority areas. A list of category Z services is appended to this strategy at appendix 3. To enable the forward plans to be achievable it is essential that the category Z savings are managed out within the identified timescales, in the event that this is not possible, alternative proposals will need to be identified and approved by members as part of the prioritisation process.

The savings within non-priority areas identified in October 2004 are included within appendix 3.

Principle 2 - Manage financial resources to achieve efficiency and "Value for Money"

(incorporates former Strategy 3)

To ensure that available resources are used to best effect, the Council is continuing to develop its Corporate and Service Planning approach. This approach includes the following.

Delegation of Budget Management

Budget management will be delegated to individual service managers, subject to appropriate training and internal controls being put in place. The training proposals and internal controls are currently under development and it is planned to fully implement this approach during the current service planning cycle. This approach is being adopted to enable responsibility and accountability for delivering services within agreed resource levels to be placed at the heart of service delivery and achieve improved outcomes for service users. It is important that Service Managers take a medium term view of their service and in so doing, bid for appropriate and realistic levels of funding by presenting robust service plans and any additional requests for funding will be supported by valid business cases. Once the service budget has been approved, Service Managers will need to operate within the approved budget and utilise virement sparingly but effectively to provide the flexibility to deliver service outcomes efficiently.

Benchmarking and identifying efficiency gains

In response to the "Gershon Agenda" or local efficiency agenda and to ensure Value for Money is achieved, the Council will develop a robust benchmarking approach which will need to be embedded across the organisation. This will support the ongoing search for efficiency gains.

The aim of the local efficiency agenda is to ensure that resources available to local government are used in the optimum way to deliver better public services according to local priorities. All local authorities are expected to achieve the following targets:

- Total efficiency gains equal to at least 2.5% of their 2004/5 baseline expenditure by the end of 2005/6 and 5% by the end of 2006/7 and 7.5% by end of 2007/8
- Cashable efficiency gains equal to at least 1.25% of their 2004/5 baseline expenditure by the end of 2005/6, 2.5% by the end of 2006/7 and 3.75% by end of 2007/8.

The Council's Annual Efficiency Statement, which sets out the annual efficiency target together with the detail of how the target will be achieved is produced in April each year and submitted to the Department of Communities and Local Government (formerly the Office of the Deputy Prime Minister). The Council's revised forecast for the three year 2005/6 to 2007/8 is £1,087,000 efficiency gains of which £543,500 is cashable[2].

All services are currently subject to a review, as part of the service planning and budget development process, in terms of costs, performance and quality. Scrutiny mechanisms are also in place, these include Member Development and Scrutiny panels, internal and external audit, Constitution and Accounts Committee and "Gateway Reviews" of individual service plans.

During the last financial year service managers were asked to identify a 5% efficiency target as part of the service planning approach. It is proposed that in the future efficiency gains are stepped to take account of priorities and value for money analysis but should target to achieve an overall efficiency of 5%.

Principle 3 - Maintain flexibility to respond to a changing local government environment

The Medium Term Financial Strategy is and will continue to be influenced by changing national and regional policies. A degree of flexibility needs to be allowed in allocating resources outside the annual budget process. This principle should be established in response to rapid change, national constraints, new Government regulation and direction. The risk and uncertainty of managing the Council needs to be counter-balanced with some spare capacity and contingent resources. The section on Managing the Council's Assets, Reserves and Balances also addresses with this issue.

[2] Cashable – result of a direct financial saving or benefit, with money released that can be spent elsewhere or recycled within a service to deliver better results

"Horizon scanning" should be ongoing particularly in light of the Comprehensive Spending Review 2007 (CRS07). Early indications are that the CSR07 will be a zero based review across the whole of government. Whilst there have been a number of spending reviews this is the first comprehensive review in ten years. At this stage, it is likely that Local Government will maintain a real terms neutral position. However, in terms of district councils it is likely that this will result in a decrease in real terms, as districts do not deliver the highest government priorities such as Education and Adult Social Services. Themes being considered as part of the CSR07 include the review of the level of balances and reserves; asset management and surplus assets; and efficiency and shared services.

In 2003/4 the Council set up a capacity building a priority setting reserve. In addition, to enable the Council to optimise gains from specific initiatives within the changing environment it is appropriate to provide for an "Invest to Save" budget in the Council's Revenue budget in the future to enable the flexibility to target resources where there is an opportunity to invest some revenue funding to make efficiency gains for the future or save in the longer term. Access to the "Invest to Save" budget would be by submission of a business case.

Principle 4 - Maintain a sustainable Revenue Budget

This strategy addresses the issues relating to the resource requirement to deliver the Council's Corporate Plan and Annual Performance Plan. The strategy makes more active use of resources to meet the vision of the Council and Government requirements over the next five years.

When closing the Accounts for 2005/6 the Council has adopted an accounting policy of maintaining a General Fund working balance of between 4% to 5% of gross turnover or between 10% - 15% of net expenditure to provide adequate cover for any unanticipated expenditure or loss of income that may occur over the course of the financial year.

The Council has identified a desire to move towards adopting zero based budgeting principles. This will be done on an incremental basis, by introducing activity based costing, incorporating value for money benchmarking into service planning and requiring the demonstration of a sound business case to support requests for funding.

Whilst there is a need to consider the longer term forecast of the impact of corporate demands it is essential that this is also reviewed annually as part of the budget setting process. The following corporate demands have been identified for 2007/8:

- Overall inflation based on Retail Price Index 2.4% (June 2006)
- Energy costs current rate of inflation around 25%. The Council has fixed price contracts for gas and electricity, although these expire during 2007/8, although a new contract will be rigorously negotiated it is likely that inflation rate will need to exceed that of RPI, say 25%.
    - Electricity 1 year contract with NPOWER expires 31/3/07
    - Gas 2 year contract with Scottish and Southern power expires 30/11/07
- The current 3 year pay settlement comes to an end at the end of the current financial year, negotiations are due to commence in the Autumn. The Chancellor has urged that public sector pay settlements are kept low for the purposes of budgeting it is proposed that the inflation rate be based on RPI
- The Pension Actuary has undertaken a review of the pension fund and SKDC's sub fund is currently 88% funded.
- The Leisure Contract is due to expire in March 2008. Whilst the Council has agreed to proceed with the creation of a Leisure Trust it is also continuing with a concurrent procurement process for the delivery of leisure service in the event that the creation of a robust Trust business plan is not satisfactory. There are a number of financial implications which are under consideration and will be further developed as part of the business planning and budget setting process for 2008/9.
- The initial impact of the introduction of the enhanced Concessionary Travel – Bus Pass scheme with effect from 1st April 2006 has been assessed. There has been an increase in take-up and use of the free bus pass, projections have been done based on the first two months of the financial years as shown below. In addition, it was announced in the budget that the scheme will be extended on a national basis from 2008, although it is currently unclear how this will be administered and whether it will impact of formula grant, therefore, the Council will need to keep this area under review.

	April tickets	May tickets	Annual tickets	Cost £k
2005	17,142	16,225	210,585	106
2006	24,969	25,611	316,000 projected	335 projected
Increase	7,827	9,386	105,415	229

The district has one of the fastest growing populations in the country, which should be reflected in the Tax Base (although this will be partly reflected in relatively lower Formula Grant). The Council has agreed to a review of the assumptions used to assess the Tax Base and Collection fund as follows:

- The estimated number of properties (in Band D terms) expected to be added for the period of the budget
- The collection rate assumptions
- The balance on the Collection Fund

Although the financial benefit from the above actions may not be major, it will enable the resource base to be increased in a sustainable way.

The medium term financial strategy will need to be amended to reflect the outcome of the ballot of Tenants on Large Scale Voluntary Transfer (LSVT). At this stage it reflects policy proposals and decisions to date should the Tenants vote to proceed with the Council's preferred option of LSVT. In particular, it provides for:

- The impact of diseconomies of scale arising from LSVT to be managed out over a five year period post transfer
- The General fund be protected by utilising interest receipts generated from LSVT capital receipts based on a phased capital programme
- The Capital programme be phased over 5 years for Affordable Housing utilising 50% of the net useable receipt and 10 years for Developing Sustainable Communities utilising 50% of the net useable receipt, with an annual review to ensure that the Council remains protected from the impact of LSVT.

Principle 5 – Maintain a prudent approach when making estimates of external funding from Government (formerly referred to as strategy 1)

In 2003/4, the Council benefited from the methodology changes for the distribution of formula grant. In 2004/5 further changes to the grant system caused further difficulties in assessing the grant settlement, in particular the switch in funding source for housing benefit administrative grant from the ODPM to DWP. On a like for like basis the general level of grant received was a 2.3% increase; below the rate of general inflation. For 2005/6 the formula was more consistent than in the previous 2 years, although the capping criteria was harsher.

In 2006/7, the Government introduced a new system to distribute grant to local authorities – Under the new system the distribution of grant is determined by four elements known as the 4 block grant distribution system. The previous system involving the use of Formula Spending Share has been removed. The four elements are the Relative Needs Formulae (RNF); a Relative Resource Amount; a central allocation (an amount per head) and a floor damping scheme. The Council's formula grant for 2006/7 was £9.27m, this was an increase of 3.3% on 2005/6 on a like for like basis. The settlement provided for new money for the extension of concessionary travel from half to free fares for the over 60s and qualifying disabled. The funding was included in the level of formula grant received and cannot be separately identified.

Following the 2006 budget announcement of the introduction of free national bus travel during off peak times for the qualifying group referred to above with effect from April 2008, it is unclear at this stage how this scheme will be administered and how this will impact on the level of grant settlement in future years, therefore, the Council has agreed to ask officers to keep this under review until the outcome is known.

Also in 2006/7 the Government for the first time provided an 'indicative allocation' for more than one year ahead. The indicative allocation for 2007/8 was £9.626m. The Government has confirmed that, with its next comprehensive spending review (CSR07), it intends to move to announcing figures for 3 financial years as part of future years' grant settlements, starting with an announcement in 2008/9. Whilst this will enable more robust forward planning of the MTFS, as referred to in the text associated with principle 3 above, it is likely that future settlements for districts will result in a decrease in real terms, as a result of the CSR07.

Taking account of the forgoing the assessment of future levels of government grant is always difficult although the table below sets out potential position for SKDC over the next five years (assumes inflation at 2.4% based on RPI wef 2009/10).

Final settlement 2006/7 £m	Indicative settlement 2007/8 £m	Assumed settlement 2008/9 £m	Assumed settlement 2009/10 £m	Assumed settlement 20010/11 £m	Assumed settlement 20011/12 £m
9.272	9.626	9.626	9.857	10.093	10.336

Sir Michael Lyons is undertaking a review of the function and funding of Local Government. The final report is due in December

2006, this is likely to affect the Council's MTFS in the future, particularly in relation to the ability to raise local income.

Specific grants - Local authority business growth initiative (LABGI) was introduced in 2005/6. This grant relates to promoting economic growth of the area by allowing Council's to retain a proportion of any increase in business rate revenue, above a certain level. It can be used to support any Council expenditure, the Council has approved that LAGBI grant be used to support the overall expenditure of the Council, in particular as Town Centre Development has already been identified as category A priority and is therefore receiving additional funding to support stepped improvement in performance. Grant will be awarded in the last quarter of the financial year based on the actual changes to rateable values in the previous calendar year, subject to a review of the outcomes at the end of year one. The level of grant awarded for 2005/6 was £377k.

Principle 6 -Identify and seek opportunities for external funding whilst maintaining prudent estimates of realisable funding (formerly referred to as Strategy 4)

This continues the strategy 4 of the Council's previous MTFS – "The Council must continue to find new sources of funding for its activity." This strategy was adopted in light of the fact that Government funding continues to be 'top-sliced' for specific projects. The council's policy is that if a specific scheme links with the Council's priorities then bids should be submitted.

The secured use of section 106 agreements have and continue to help develop community assets with less reliance upon the Council's own resources. It is essential that a database of section 106 agreements is maintained and managed to ensure that the community benefits are realised in line with the agreements made.

Examples of the council's successful access to additional external funding include:

- DEFRA funding to support the development of the Council's recycling priority
- Planning Delivery Grant for improved performance in line with the Council's category B priority at that time

The Council, along with other Lincolnshire Districts and the County Council have entered into a Public Service Agreement (round 2) and may receive performance reward grant if it cn demonstrate achieving 'stretch' targets in line with the PSA. Service Managers will need to ensure the achievement of these targets is built into their service plans.

The medium term financial issues arising from additional funding streams are:

- If commitments are made that extend beyond the period or amount of grant funding and appropriate exit strategy or sustainability plan is put in place
- When integrating various funding streams into their programme delivery, Service Managers need to be clear about:
    - The use and timespan of that funding; and
    - The outputs and outcomes required as a result of receiving that funding

A review of the current position relating to Performance Grants, Challenge Funding and Partnership contributions will be undertaken during the remainder of the current financial year.

Principle 7 - Manage the Council's Assets, Reserves, Balances and Receipts to optimise financial returns for future investment in the Council's priorities for the benefit of the community (formerly referred to as strategy 5)

The Council has reviewed its Asset Management Plan during 2006 and will be reviewing is Capital Strategy and Treasury Management Strategies during the Autumn of 2006. These reviews have and will be undertaken on the basis of ensuring that financial returns for future investment in Council priorities are optimised for the benefit of the community.

The Asset Management Plan is the core document identifying those assets either not being fully utilised or those that are surplus to requirements. The Capital and Asset Management Performance Group evaluate operational issues arising from the AMP and feeds them back to the Management Board and Cabinet.

Reserves can be held for three main purposes:

- A working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this forms part of general reserves
- A contingency to cushion the impact of unexpected events or emergencies – this also forms part of general reserves
- A means of building up funds often referred to as earmarked reserves to meet known or predicted liabilities.

Whilst it is primarily the responsibility of the council and its section 151 officer to maintain a sound financial position, external auditors have a responsibility to review the arrangements in place to ensure that financial standing is soundly based. In the course of their duties external auditors review and report on the level of reserves taking into account their local knowledge of the council's financial performance over a period of time. The Annual Audit Letter and Use of Resources Assessment identified that "comparatively levels of reserves and balances are high and are in need of review to ensure they remain appropriate under current circumstances". It is also likely that a theme of the CSR07 will be a review of balances and reserves, asset management and surplus assets.

A schedule of reserves and the purposes for which they are held is attached at appendix 4. A review of the level of balances and reserves was undertaken as part of the closure of accounts and preparation of Annual Statement of Accounts for 2005/6. Details of the level of reserves and current estimated movements on reserves for 2006/7 are contained in Appendix 5. The level of individual reserves was reviewed to take account of potential future use and particularly those, which are earmarked for specific purposes.

During the next financial year the Council will develop a clear protocol for the use of each reserve which will build on the attached schedule by:

- Identifying how and when the reserve can be used (based on the above rationale
- Further develop procedures for the reserve's management and control
- Further develop a process and timescale for the ongoing review of each reserve to ensure continuing relevance and adequacy.

Principle 8 - Maintain a robust Capital Strategy to support a deliverable medium term capital programme (incorporates former strategy 9)

The Council's Capital Strategy is being reviewed and will be submitted for approval during the Autumn of 2006. The existing strategy covers the period 2003 to 2006. The new strategy will fully address the new system of capital finance controls set out in the Prudential Code for Capital Finance in Local Authorities (the code).

The professional code of practice sets out a framework for self-regulation of capital spending, in effect allowing councils to invest in capital projects without any limit as long as they are affordable, prudent and sustainable. The Code allows the council to determine the appropriate level of capital investment to properly deliver quality public services, subject to affordability.

To facilitate the decision making process and support capital investment decisions the Prudential Code requires the Council to agree and monitor a minimum number of prudential indicators. These indicators are mandatory, but can be supplemented with local indicators if this aids the interpretation and many will cover three years forward. The indicators cover capital expenditure, affordability, prudence, external debt and treasury management. A copy of the prudential indicators for 2006/7 is attached at appendix 6 – entitled "Capital Finance Report". The indicators are purely for internal use by the council and are not to be used as comparators between councils, as any comparisons will be meaningless. The indicators should not be taken individually, but rather there will be benefit from ongoing monitoring of trends over time and year on year changes.

In addition, the revised Capital Strategy will set out the Council's approach to capital investment and will result in the development of a medium term capital programme based on a forward five-year view. All capital schemes will be appraised and scored when developing the medium term capital programme, however, it is essential that the process is flexible enough to deal with emerging or urgent schemes, this will be addressed in the revision of the Capital Strategy.

The Capital Strategy will need to be kept under review to ensure it remains 'fit for purpose', in particular, a review will be required following the impact of the ballot of Tenants on LSVT, although principle 4 above has referred to the approved use of a potential transfer receipt in relation to the development of the capital programme and the need to protect the general fund from the impact of LSVT.

Principle 9 - Improve Treasury Management Performance **(formerly referred to as strategy 6)**

Treasury Management is the management of cash and working capital, including both short term cash and long term funds. The Council has an integrated treasury management strategy and has adopted the CIPFA Code of Practice for Treasury Management in the Public Services. The Capital Finance report referred to in the above section refers to specific Treasury Management issues.

The Council has currently maintained a flexible approach to debt redemption and borrowing. It has previously been agreed that regular reports will be presented to the Constitutional and Accounts Committee on performance.

Treasury Management is an important element within the value for money assessment. The Council has been repaying debts for a number of years and is left with a low level of debt but at 'relatively' high interest rates. If this is repaid early the Council will pay a premium for doing so, hence the current policy of repaying on maturity.

Given that the Council is looking to enhance its capital programme, the Prudential Code will be used to ensure the decisions made with regard to borrowing reflect affordability, sustainability and value for money. This will involve consideration of the following issues:

- Balancing investment income against new borrowing, ie it may be cheaper to bring back investments to fund new capital expenditure
- Leasing versus buying outright
- Ensuring that the balance of investment between General Fund and Housing Revenue Account is well defined and analysis of the impact of changes of debt and investment structure on both funds. This is particularly relevant to the proposals on LSVT.

The current investment strategy is relatively cautious, and whilst it is respected that the Council will wish to be risk averse with regard to capital investment, there are opportunities to grow the returns from investments without undue risk.

The existing strategy should be widened to include alternative options available with and without housing stock transfer. The development of the strategy will also require the development of a longer-term Capital Programme, and a clearer link to the budget process so that resource base can be updated to include the best estimate of investment returns.

To develop the Treasury Management function within the Council, additional capacity is planned within Financial Services with the creation of an Exchequer function and also the Council has engaged external advisors who will:

- Complete an overview of the Council's financial position with regard to its strategy and objectives, including an analysis of the Council's Consolidated Balance Sheet and relationship of borrowing to the Capital Financing Requirement. An examination of future year's forecasts and the implications for the debt and investment portfolios will also be undertaken and fed into an annual review of the Council's Treasury Management Strategy
- Undertake Interest Rate Forecasting and Economic Advice
- Undertake an analysis of the variable debt portfolio with reference to its structure and volatility
- Undertake a review of debt structuring
- Provide technical advice
- Assist with the annual treasury management report and stewardship statement
- Provide advice, assistance and recommendations relating to CIPFA Code of Practice and the Prudential code
- Review the Council's investment strategy to ensure compliance with Investment Guidance from the Department of Communities and Local Government

The MTFS will be updated to reflect the outcome of this work.

Principle 10 – Balance the need to meet local taxation demands with Community aspirations and ability of local taxpayers to meet them (replaces former strategy 8)

The Council currently has the 2nd lowest council tax in Lincolnshire, the 5th lowest tax of the 28 authorities in the East Midlands and is in the lowest 30 in the Country. Historically the council has been a low spend low tax authority. The Council is committed to achieving high quality and high performing services. The Corporate Plan currently in development acknowledges the need to spend more in order to improve the Council's status as a service deliverer and enabler.

With Government grant likely to reduce in real terms and spending already at a low level, the Government policy to keep tax increases from year to year at a modest level (5% for 2006/7) means that the Council is working from a relatively low resource base, therefore, all potential income streams need to be considered. In keeping with recent years it is likely that the level of Council Tax increase acceptable to Government will need to be limited to an increase of less than 5% taking account of the current capping regime. The table[3] below sets out an indicative SKDC and Special Expenses budget requirement to be funded from Council Tax.

2006/7 £m	2007/8 £m	2008/9 £m	2009/10 £m	2010/11 £m	2011/12 £m
5.144	5.466	5.795	6.145	6.514	6.907

Principle 11 - Maintain a robust Fees and Charges Strategy (formerly strategy 7)

The Council has recently approved the development of a Fees and Charges Strategy to address both discretionary and mandatory fees over a rolling three year period. This will be approved in Autumn 2006 and should be read in conjunction with the MTFS.

The strategy will review all income options taking into account the impact on service users' in terms of affordability and accessibility. It will identify the schedule of charges, the date of revision, and the basis of calculation and take account of the Local Government Act 2003, which permits Council's to charge for further areas. In addition, the strategy will need to address the final outcome of the Lyons Review in relation to the ability to raise local income.

Principle 12 – Manage the impact of the introduction of Local Area Agreements

SKDC and other Lincolnshire Councils are in the final phase of the first round of Local Area Agreements (LAAs). The Local Area Agreement is currently under development and negotiation. It is essential that the impact of the introduction of LAAs is fully understood and managed to enable the funding outcomes to be incorporated into future revisions of the MTFS.

[3] Assumes a maximum of 5% tax increase and 1% increase in taxbase

Principle 13 – Deliver the priorities of the Council without exposing the Council to unnecessary risks by targeting the use of resources linked to an assessment of corporate risk

SKDC is enhancing its approach to managing risk both at a strategic and operational level. Mechanisms are currently in place to manage strategic risks through a regular ongoing review of the Strategic Risk Register by the Management Board. In addition, the service planning template incorporates a risk assessment to be completed by Service Managers. Further work is ongoing to embed risk management across the authority.

There is a need to ensure that the Council is not exposed to unnecessary risks by adopting a policy of targeting the use of resources linked to an assessment of corporate risk and ensuring that appropriate mechanisms are in place to monitor the effectiveness of this approach and ensure that it is being embedded. The mechanisms will include a greater emphasis on risk assessment in the preparation of requests for resources through the service planning and budget process.

Principle 14 – Manage the financial viability of the Housing Revenue Account (HRA) and ballot tenants on the preferred option of LSVT to provide the investment required to deliver Tenant aspirations (incorporates former strategy 10)

The Council is required to produce a 30 year business plan for the HRA, this was done as part of the stock option appraisal process and enabled a full financial assessment of the HRA. Taking account of the consultation with tenants and their identified aspirations for investment in improvements to their homes and the level of service, LSVT was identified as the preferred option for the future ownership and management of the Council's housing stock. A ballot to the tenants is planned for late Autumn 2006.

The MTFS will need to take account of the outcome of the ballot, in that, if the transfer proceeds the impact of transfer is managed within the overall strategy as identified in this strategy; or if the transfer does not proceed a review of the HRA business plan is undertaken to establish the degree of tenant aspirations that can be afforded with the lower level of resources that would be provided by the HRA.

In the interim, the financial viability of the HRA should be managed and maintained within government guidelines.

Appendix 1 – Category B Priorities for incremental improvement

- Street scene
- Business development
- Diversity
- Housing Management
- Local Strategic Partnership and Community Strategy
- Maintenance of Council Assets

Appendix 2 – Category M priorities for maintained performance or statutorily defined level

- Arts
- Building control
- Business management
- Business Rates
- Car parks
- Emergency Planning
- Environmental Health (statutory requirements)
- Human Resources
- Housing Repairs
- Legal and Administration
- Leisure
- Licensing
- Markets
- Parks
- Public Conveniences
- Public Transport (statutory requirements)

Appendix 3 – Category Z projected annual savings

Projected Category Z savings based on 2004/5 base year						
Service	**Proposal**	**Year 1 2005/6 £k**	**year 2 2006/7 £k**	**year 3 2007/8 £k**	**year 4 2008/9 £k**	**year 5 2009/10 £k**
Pest control	Full cost recovery	125	125	125	125	125
Travel vouchers	Restrict eligibility for new applicants	0	16	32	47	63
Rural routes	Terminate subsidy on rural routes	36	36	36	36	36
Discretionary rate relief	Develop new scheme	0	84	84	84	84
Business support grants	Terminate current scheme but create new scheme encouraging inward investment	50	50	50	50	50
Grants to Arts, Leisure & Housing orgs	Terminate current scheme but create new scheme established under vulnerable persons priority	11	11	11	11	11
Historic Building Grants	Terminate schemes	20	20	20	20	20
LCC recreation grants	Reduce contribution to 16.6% and max budget of £25k with no funding to schemes not supported by LCC	25	25	25	25	25
Archaeology services	Reduce contract to meet only statutory obligations	13	13	13	13	13
Tourism	Continue to provide TIC at Grantham & Stamford but curtail investment in strategic toursim development	78	78	78	78	78
Annual sub total		358	458	474	489	505
Parish council election exes	Re-charge Parish election exes to parish councils in years of election			6		
Annual total		358	458	480	489	505

Appendix 4 –Schedule of Reserves

Category of earmarked reserve	**Rationale**
Insurance Reserve (Revenue)	A high level of 'Self-insurance' is a mechanism used by the Council to reduce external premiums. Sums are held in this earmarked reserve to meet potential and contingent liabilities.
Pension Reserve (Revenue)	**Former Employees** – This reserve provides for matching added years payments in respect of former employees. The Council does not currently operate a policy for added years and this reserve will reduce over time. **Current Employees** – This reserve is used to finance the capital costs of early retirement decisions taken by the Council and to help protect the Council from large changes in Council Tax resulting from unanticipated rises in the employer's contribution rate following the triennial valuation
Building Control (Revenue)	Annual surpluses from the chargeable element of Building control activities are set aside in this reserve and it is then used to finance service improvements and offset any future deficits
Stock Option Ballot Reserve (Revenue)	This reserve has been set up to offset any abortive costs arising from the forthcoming ballot of Tenants, to protect any impact on the General Fund. Consideration of the reserve will be made post ballot, with any abortive costs being offset against it or in the event of a positive ballot the future use of the reserve will be determined as any costs of transfer will be offset against the transfer receipt at the point of transfer.
Capacity building, priority setting and service improvement reserve (Revenue)	This reserve has been created to finance stepped improvements required for delivery of the Council's priority services and support the creation of additional corporate capacity.
Major Repairs Reserve (Capital)	This is the mechanism whereby the Council is required to account for the resources provided through the Major Repairs Allowance, which is provided through Housing Revenue Account Subsidy and is available to fund capital expenditure on HRA assets.
General Fund (Capital reserve)	This reserve is earmarked to finance the Council's future capital programme

Balances	
Housing Revenue Account (HRA)	The HRA is maintained in accordance with the Local Government and Housing Act 1989 which sets out the framework for "ring-fencing" the HRA. The account has to be self financing and there is a legal prohibition on cross subsidy to or from the General Fund
General Fund	Council has approved the policy of maintaining a General Fund working balance of between 4% to 5% of gross turnover or between 10% - 15% of net expenditure to provide adequate cover for any unanticipated expenditure or loss of income that may occur over the course of the financial year
Collection Fund	The balance on the Collection Fund is available for financing the expenditure of Lincolnshire County Council, Lincolnshire Police Authority and SKDC

Appendix 5 – Movements in Reserves

	Balance as at 1 Apr 06 £'000	Movements in Year £0	Balance as at 01-Apr-07 £'000	Movement in Year £'000	Balance as at 1 Apr 08 £'000	Movement in Year £'000	Balance as at 1 Apr 09 £'000	Movement in Year £'000	Balance as at 1 Apr 10 £'000	Movement in Year £'000	Balance as at 1 Apr 11 £'000
Capital Reserves											
General Fund Capital Reserve*	5057	(5,057)	-	0	-	0	-	0	-	0	-
Major Repairs Reserve	9124	(917)	8,207	(1,000)	7,207	(1,000)	6,207	(1,000)	5,207	(1,000)	4,207
	14181	(5,974)	8,207	(1,000)	7,207	(1,000)	6,207	(1,000)	5,207	(1,000)	4,207
Specific Revenue Reserves											
Insurance Reserve	500	0	500	0	500	0	500	0	500	0	500
Building Control**	412	(50)	362	(50)	312	(50)	262	(50)	212	(50)	162
Capacity Building, Priority Setting			-								
and Service Improvements	1810	(1,200)	610	(250)	360	(250)	110	(250)	- 140	(250)	- 390
Stock Option Ballot Reserve	802	(400)	402	0	402	0	402	0	402	0	402
Pensions Reserve - Former Employees	307	(65)	242	(65)	177	(65)	112	(65)	47	(65)	- 18
Pension Reserve - Current Employees	2116	(800)	1,316	(200)	1,116	(200)	916	(200)	716	(200)	516
	5947	(2,515)	3,432	(565)	2,867	(565)	2,302	(565)	1,737	(565)	1,172
Balances											
General Fund	2000	0	2,000	0	2,000	0	2,000	0	2,000	0	2,000
Housing Revenue Account	6045	694	6,739	1,383	8,122	1,000	9,122	800	9,922	600	10,522
	8045	694	8,739	1,383	10,122	1,000	11,122	800	11,922	600	12,522

* Use of General Fund Capital Reserve will be dependant upon realising capital receipts for East Street and also decisions regarding prudential borrowing

** Building Control service plan to identify controlled use of reserve over the next 5 years

Appendix 6 – Prudential Indicators – Capital Finance Report

1. In accordance with the CIPFA - Prudential Code for Capital Finance in Local Authorities and the Local Government Act 2003, the following indicators meet the requirement.

2. The actual capital expenditure that was incurred in 2004/05 and the estimates of capital expenditure to be incurred for the current and future years that are recommended for approval are:-

Capital Expenditure					
	2004/2005 £000 Actual	2005/2006 £000 Estimate	2006/2007 £000 Estimate	2007/2008 £000 Estimate	2008/2009 £000 Estimate
Housing General Fund	330	300	350	350	350
Community DSP	210	131	360	110	-
Economic DSP	163	1075	3900	1500	1000
Engagement DSP	-	571	770	-	-
Healthy Environment	1477	290	2700	-	-
Resources	774	58	560	560	-
Total Other Services	2954	2425	8590	2520	1350
Housing Revenue Account	5022	4452	5017	6020	5853
Total Capital Programme	7976	6877	13607	8540	7203

3. Estimates of the ratio of financing costs to net revenue stream for the current and future years, and the actual figures for 2004/2005 are:-

Ratio of financing costs to net revenue stream					
	2004/2005 Actual	2005/2006 Estimate	2006/2007 Estimate	2007/2008 Estimate	2008/2009 Estimate
Non-HRA	-2.05	-2.21	-1.12	-0.75	-0.29
HRA	-3.08	-1.78	-1.86	-1.76	-1.28

The estimates of financial costs include current commitments and the proposals in this budget report.

4. Estimates of the end of year Capital Financing Requirement at 31 March 2005 are:-

Capital Financing Requirement					
	31.03.05 £000 actual	31.03.06 £000 Estimate	31.03.07 £000 Estimate	31.03.08 £000 Estimate	31.03.09 £000 Estimate
Non-HRA& HRA	8	8	8	8	8

5. The Capital Financing Requirement measures the authority's underlying need to borrow for a capital purpose. In accordance with best professional practice, South Kesteven District Council does not associate borrowing with particular items or types of expenditure. The authority has an integrated treasury management strategy and has adopted the CIPFA Code of Practice for Treasury Management in the Public Services. South Kesteven District Council has, at any point in time, a number of cashflows both positive and negative, and manages its treasury position in terms of its borrowings and investments in accordance with its approved treasury management strategy and practices. In day to day cash management, no distinction can be made between revenue cash and capital cash. External borrowing arises as a consequence of all the financial transactions of the authority and not simply those arising from capital spending. In contrast, the Capital Financing Requirement reflects the authority's underlying need to borrow for a capital purpose.

6. CIPFA's Prudential Code for Capital Finance in Local Authorities includes the following as a key indicator of prudence:-

"In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that net external borrowing does not, except in the short term, exceed the total of capital Financing Requirement in the preceding year plus the estimates of any additional Capital Financing Requirement for the current and next two financial years".

I report that the authority had no difficulty meeting this requirement in 2004/2005, nor are any difficulties envisaged for the current or future years. This view takes into account current commitments, existing plans, and the proposals in this budget report.

7. In respect of its external debt, it is recommended that the Council approves the following Authorised Limits for its total external debt gross of investments for the next three financial years, and agrees the continuation of the previously agreed limit for the current year since no change to this is necessary. These limits separately identify borrowing from other long term liabilities such as finance leases. The Council is asked to approve these limits and to delegate authority to myself within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities, in accordance with option appraisal and best value for money for the authority. Any such changes will be reported to the Council at its next meeting following the change.

Authorised limit for external debt				
	2005/2006 £m	2006/2007 £m	2007/2008 £m	2008/2009 £m
Borrowing	30	30	30	30

8. I report that these Authorised Limits are consistent with the authority's current commitments, existing plans and the proposals in this budget report for capital expenditure and financing, and with its approved treasury management policy statement and practices. I confirm that they are based on the estimate of most likely, prudent but not worst case scenario, with in addition sufficient headroom over and above this to allow for operational management, for example unusual cash movements. Risk analysis and risk management strategies have been taken into account; as have plans for capital expenditure, estimates of the Capital Financing Requirement and estimates of cashflow requirements for all purposes.

9. The Council is also asked to approve the following Operational Boundary for external debt for the same time period. The proposed Operational Boundary for external debt is based on the same estimates as the Authorised Limit but reflects directly my estimate of the most likely, prudent but not worst case scenario, without the additional headroom included within Authorised Limit to allow for example for unusual cash movements, equates to the maximum of external debt projected by this estimate. The operational Boundary represents a key management tool for in year monitoring by myself. Within the Operational Boundary, figures for borrowing and other long term liabilities are separately identified, The Council is also asked to delegate authority to myself, within the total Operational Boundary for any individual year, to effect movement between the separately agreed figures for borrowing and other long term liabilities, in a similar fashion to the Authorised Limited. Any such changes will be reported to the Council at its next meeting following the change.

Operational Boundary for external debt				
	2005/2006 £m	2006/2007 £m	2007/2008 £m	2008/2009 £m
Borrowing	7	6	5	4

10. The Council's actual external debt at 31 March 2005 was £7 million. It should be noted that actual external debt is not directly comparable to the Authorised Limit and Operational Boundary, since the actual external debt reflects the position at one point in time.

11. In taking its decisions on this budget report, the Council is asked to note that the Authorised Limited determined for 2006/2007 (see paragraph 3 above) will be statutory limit determined under section 3(1) of the Local Government Act 2003.

12. The Band D Council Tax that would result for South Kesteven District Council for 2006/2007 from the totality of the capital and revenue plans recommended in this budget report is £105.66.

The estimate of the incremental impact of capital investment decisions proposed in this budget report, over and above capital investment decisions that have previously been taken by the Council are:

for the Band D Council Tax

2006/2007	2007/2008	2008/2009
£2.00	£4.00	£4.98

for average Housing Rents

2006/2007	£2007/2008	2008/2009
£ -	£ -	£ -

14. In considering its programme for capital investment, the Council is required within the Prudential Code to have regard to:

- Affordability, eg implications for Council Tax.
- Prudence and sustainability, eg implications for external borrowing.
- Value for money, eg option appraisal.
- Stewardship of assets, eg asset management planning.
- Service objectives, eg strategic planning for the authority.
- Practicality, eg achievability of the forward plan.

15. A key measure of affordability is the incremental impact on the Council Tax, and the Council could consider different options for its capital investment programme in relation to their different impact on the Council Tax.

16. South Kesteven District Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Services.

17. It is recommended that the Council sets an upper limit on its fixed interest rate exposures for 2006/2007,2007/2008 and 2008/2009 of 75% of its net outstanding principal sums.

18. It is further recommended that the Council sets an upper limit on its variable interest rate exposures for 2006/2007, 2007/2008 and 2008/2009 of 25% of its net outstanding principal sums.

19. This means that I will manage fixed interest rate exposures within the range 70% to 80% and variable interest rate exposures within the range of 20% to 30%. This is a continuation of current practice.

20. It is recommended that the Council sets upper and lower limits for the maturity structure of its borrowings as follows.

Amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate.

	Upper Limit
Under 12 months	11%
12 months and within 24 months	11%
24 months and within 5 years	33%
5 years and within 10 years	16%
10 years and above	28%

21. The Council has agreed a policy on the investment of sums for period longer than 364 days.