MEDIUM TERM FINANCIAL STRATEGY AND FORECAST

2020/21 – 2023/24

"Great Place, Great Community, Great Future"

EXECUTIVE SUMMARY

1. The Medium Term Financial Strategy was last presented to Executive in July 2016. Since then the Council's finances have been transformed with income increasing from property, underspends on most services and excellent collection rates on both Business Rates and Council Tax. However this should not be taken to mean the Council's financial problems are solved. The Council is now dependent on property income for services and is therefore exposed to risks in the wider economy, especially around retail. Government funding is likely to fall as are grants from partners and inflation, particularly its impact on wage costs, is beginning to bite. In addition demand for services and investment, especially in Camberley Town Centre, continues to rise. All this means that there is now a new set of financial challenges which this strategy seeks firstly to try and quantify and then seek to address.

2. It is important to remember that this report is not a blueprint for setting the budget but rather a prediction based on the facts as known now coupled with a number of assumptions. Estimates of Council Tax or pay growth are merely that – estimates – and are not to be taken as policy. This will be determined by Members, guided by Government, through the budget setting process in due course.

3. Council funding beyond 2019/20 is still not known. Although the Government has said it intends rollout 75% Localisation of Business Rates in 2020/21 the details of how this will work in a general sense have only just been released. No information is available as to what this means for individual Councils. In addition the "Fair funding review", and Business Rates rebasing and revaluation, are also likely impact the Council's funding. For the purposes of this forecast it has assumed that Surrey Heath Borough Council will at least start with its share of business rates as per the 2015 settlement but that this will reduce over time.

4. The Council is under a legal duty to set a balanced budget each year and there are various statutory safeguards in place to ensure that this happens. For example if a Council tries to set an unbalanced budget the auditor is obliged to report on this and any precept levied is likely to be illegal. A more well-known safeguard, due to recent events in Northampton, is the serving of a Section 114 notice by the Sec 151 officer which has the effect of stopping all non-essential expenditure. This notice is served if there is a risk that the Council will spend beyond its financial resources and hence become insolvent.

5. This forecast is designed to highlight the challenges in delivering a balanced budget in the future so that action can be taken now. Potential reductions in funding, coupled with the Council's ambitious capital investment programme and volatility in income streams do have the potential to put considerable strain on the Council's finances. This may be addressed by further income generation through investment and charges coupled with greater efficiency and collaboration. However if this is not sufficient service reductions may be required.

6. The Council has already taken big steps on the road to self-sufficiency and dealing with the financial challenges it faces. These challenges were not of the Council's own making but imposed by Central Government and the Council has had to take on considerable risk to address them. These risks, especially the

dependency on property income, has meant that the Council's finances are much more volatile than in the past. Fortunately, the Council does have reserves to deal with some of this volatility for the short term but it is not immune to the ups and downs of the domestic and global economy. However had the Council not invested and therefore not taken on these risks services would have had to be reduced significantly which would have a very dramatic impact on the community. This would have impacted in particular the most vulnerable who depend on the Council's discretionary services.

7. All of the Surrey Districts have come a long way to address the problems they all face. Mostly this has been achieved through income generation from property but there have also been initiatives to work more collaboratively to reduce costs, such as through the Joint Waste Contract. Most Councils have slimmed down their workforce and office space and used technology to become more efficient. What is clear is that there is a limit to what an individual Council can achieve and eventually a different approach is needed. Combining Councils, be this through the creation of new unitaries or super districts, could deliver substantial savings to maintain services. This has to be the medium term goal for Local Government in Surrey and indeed the financial situation at Surrey CC may well precipitate this. Until then Surrey Heath will need to continue to drive efficiency and grow income through charges and investment.

BACKGROUND AND CONTEXT TO THE MEDIUM TERM FINANCIAL STRATEGY

Introduction

8. The Medium Term Financial Strategy (MTFS) sets out the financial challenges that the Council faces over the next four years and sets out a strategy for dealing with them. This builds on the strategy outlined in July 2016 the benefits of which are now being realised.

9. This MTFS endeavours to take account of all the various factors and influences that may impact on the Council for the next few years. These factors include economic conditions, Government spending plans, current expenditure patterns, inflation, capital plans, planned changes to service delivery, changing demand for services, the impact of new legislation, sources of income etc. However exact information is not always available and so a number of assumptions have been made. Hence the forecast should be seen as an indication of the Council's future financial position rather than a solid prediction.

10. The MTFS looks forward anticipating the spending pressures faced by the Council, the impact of decisions already made and those in the pipeline to give an indication of the level of future savings/income required to maintain a balanced budget. This will mean that the Council can plan ahead for future challenges now rather than waiting for when they actually arise.

11. The Council continues to be committed to maximising the use of increasingly scarce resources, directing resources towards its priorities and generating income whilst keeping Council Tax within permitted levels.

12. Over the last couple of years, the Council continued to make significant progress in the achievement of its strategic financial priorities building on work already done. This means that the Council's underlying financial position remains strong but this has been achieved by the Council accepting higher levels of risk.

13. Despite these achievements there are still significant challenges facing Council finances. For example it is not known what the impact of Business Rates localisation or "Fair Funding" will be, the retail economy is very fragile, Brexit has its own set of risks and on top of that there are financial problems at Surrey County Council which could impact us. Hence the strategy needs to remain flexible and the Council's Reserves sufficiently resilient to respond to the impact of these challenges. The Council has always managed to set a balanced budget and its financial standing is sound. However the drive for further savings and new income streams will need to continue to maintain financial stability and the ongoing provision of services to our residents.

Delivering the Council's Objectives

14. The Council has four main objectives which were refreshed last year as follows:
    - **We want to make Surrey Heath an even better place where people are happy to live**
    - **We will support and promote our local economy so that our people can work and do business across Surrey Heath**
    - **We will deliver effective and efficient services better and faster**
    - **We will build and encourage communities where people can live happily and healthily.**

15. These form the basis of the Council's Five Year Strategy and flow through to the Annual Plan each year.

Objective of the Financial Strategy

16. The objective of the financial strategy is to illustrate the financial effects of existing financial commitments over the medium term and hence to set parameters for the efficiency gains and/or income necessary to achieve a balanced budget.

NATIONAL CONTEXT

17. The 2015 Local Government finance settlement set out Council funding up to the year 2019/20. The clear direction of the settlement was to further reduce the level of Local Government funding from Central Government. A distinct change in policy was the acceptance that increasing Council Tax was seen as a way of increasing resources available to fund local services. The intention to transfer a proportion of Business Rates to local Councils, albeit with new duties, signalled that the Government felt that on a national basis local services should be paid for with local taxes. For a number of Districts, Surrey Heath included, the settlement not only took away all Government grant funding by 2017/18 but also contained an obligation to pay money to the Government from 2019/20 by the application of negative grant. Following lobbying it was announced in December 2018 that the negative grant would in fact not be applied in the last year of the settlement namely 2019/20.

18. The Government launched a “Fair Funding Review” in 2016 with the intention of changing the way Local Government finance is distributed. The outcome of this is awaited and it will be interesting to see whether the actual resources to be distributed between Councils increases or whether it is just shared out in a different way. The outcome of the Fair funding review will be one of the factors that will set the base line for the introduction of 75% localisation of business rates in 2020/21. In this new system 75% of any gains above the baseline will be retained by the Council in some way. Whilst this sounds attractive in the same year the business rates system would be “rebased” (this is where gains and losses from across the country are shared), there could also be a full revaluation and one suspects a new set of business rates reliefs for businesses. Overlaying all of this it the next Spending Review which is due in 2020 and could lead to overall cuts (or increases) in Local Government funding. What this will probably mean is that the Council is unlikely to see any increase in its funding form these sources. Although the Government has eased austerity, it is likely that any additional cash will go to areas such as the NHS and social care first as they are seen as having the greatest pressures. How all this will impact on Surrey Heath is difficult to predict, and so the following has been assumed:

- There will be no negative grant going forward.
- Councils will continue to be encouraged to increase Council Tax by the maximum allowed – for Districts 3% or £5 – whichever is the higher;
- The reductions to New Homes Bonus will continue despite the impact on house building;
- Even with the localisation of business rates the amount received will continue to fall over time as any benefit to Surrey Heath will be cancelled out by the Fair Funding Review;

Government Support

19. Central Government support including business rates has decreased from £4.2m in 2010/11 to £1.5m in 2020/21. As the 4 year settlement is not due until later in 2019 there is no certainty re future funding beyond March 2020. As a result of this all these figures are estimates.

Business Rates

20. Surrey Heath is responsible for collecting business rates, which are set centrally, from all businesses in the borough. Under the standard 50% system, 50% of all business rates collected go to the Government with 40% remaining with the borough and 10% going to the county. In two tier areas, in order to ensure that Districts did not get more money that their relative needs, a "fixed tariff" is charged against the 40% allocation which in effect means that most of it is lost. In addition, the Government sets an annual baseline as to the level of business rates it expects to be billed in the year. If the Council manages to over achieve against this target, then it can effectively keep 40% of any increase (reduced to 20% by the application of a safety net levy) with 10% going to the county and 50% to the Government. If, however, it underachieves then it will suffer 40% of the shortfall but can call on the safety net if there is a large loss. Business rates go up and down not only because businesses open and close but also due to revaluations resulting from appeals from the Valuation Office which can go back several years.

21. For 2018/19 Surrey Heath was in a 100% Surrey Business rates pilot with the County and all the districts. This means that 100% of growth, rather than 50%, is retained in Surrey and split 70:30 between the county and districts. There is also no levy charged. Sadly this scheme was not rolled over in to 2019/20 and a new application was been submitted to join a 75% pilot – however this was unsuccessful and so the Council has reverted back to the standard 50% business rates localisation, as explained above, albeit in a pool with some other Districts. This removes the safety net levy and hence retains an additional 20% of any gains locally.

22. The Government has said that it would like to implement 75% localisation by 2020/21 and potential impact of this has already been set out above. The giving of more business rates to Councils by Central Government is to be welcomed as it enables Councils to share in any growth. The downside of this is that Business rates income is more volatile, than say a direct grant, as it is impacted by the wider economy and that could impact services.

23. The 4 year settlement figures together with the projections are shown in the table below. It has been assumed that the amount of business rates the Council receives will fall over time.

Central Government Funding								
	4 year settlement - February 2016				Estimated	Estimated	Estimated	Estimated
	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
Core Funding	£0	£0	£0	£0	£0	£0	£0	£0
Revenue Support Grant	357	0	0	0	0	0	0	0
Share of Business Rates	1,435	1,464	1,507	1,543	1,250	1,000	750	500
	1,792	1,464	1,507	1,543	1,250	1,000	750	500
Other Grants rolled in:								
Transitional Grant	133	84						
	1,925	**1,548**	**1,507**	**1,543**	**1,250**	**1,000**	**750**	**500**
Reduction in funding		**-377**	**-41**	**36**	**-293**	**-250**	**-250**	**-250**

New Homes Bonus

24. Due to the success of the New Homes Bonus the Government implemented changes to the New Homes Bonus scheme in 2017 to reduce its overall cost as follows:

- For 2018/19 the incentive was to be paid for 4 years rather than the original 6;
- The first 0.4% of the tax base increase each year will not qualify for NHB. That means that the first 150 units built in the borough do not qualify for a bonus. This is likely to have a major impact on the amount of bonus received in any given year

25. Further changes relating to restrictions on NHB for homes granted on appeal or the lack of a local plan have been mooted but were not been implemented in 2019/20.

26. It is difficult to predict the future level of News Homes Bonus. Although the Government may be tempted to reduce the incentive still further they also want more houses to be delivered. Hence it has been assumed that provided houses continue to be delivered at the same rate as now the bonus will remain reasonably static.

Year		2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
		£m	£m	£m	£m	£m	£m
Estimated payment		0.864	0.521	0.400	0.400	0.400	0.400

Council tax income

27. The Local Government Settlement for 2018/19 allowed Districts to increase Council Tax by up to 3% or £5, whichever is the higher. The Government has stated this will be the limit going forward and so has been assumed in the forecast.

28. It has also been assumed that the tax base will increase by 1.0%. This is about 270 Band D properties per annum.

29. In the future the Government may allow Councils to increase Council Tax through new band or a levy but this has been ignored for forecasting purposes.

Council Tax Forecast

Year	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24
Tax base	37,540	38,054	38,435	38,819	39,207	39,599
Band D	£212.42	£218.76	£225.33	£232.09	£239.06	£246.23
Total funding	£7.974m	£8.325m	£8.661m	£9.010m	£9.373m	£9.751m

It should be noted that the figures exclude the Special Expenses charge.

It is a major element of the Financial Strategy that Council tax is increased by the maximum permitted level each year

SERVICE AND OTHER PRESSURES

Employee Costs

30. The Council has historically sought to limit the growth in salary costs by fixing in cash terms the salaries budget despite increases in wages and increments. This was achieved by greater efficiency resulting in a lower headcount. However more recently the Council has found it increasing difficult to recruit in a number of professional areas resulting in an upward pressure on wages costs. In addition further reductions in headcount are unlikely unless the Council radically changes the way it delivers services. As a result pay growth will be an ongoing budget and for the purposes of the forecast an increase of 2.0% per annum has been assumed.

31. Historically pensions have been an increasing burden on the Council. However a recent actuarial review indicated that the scheme is almost fully funded so no increase in contributions is anticipated over the life of this forecast.

Inflation

32. A number of the Council's contracts are indexed in some way to inflation. It has been assumed that these increases will be in line with CPI and this has been estimated to be 2.0% pa. Any inflation over this will need to be managed through greater efficiency and/or service rationalisation.

Reduction in Surrey County Council support

33. The Council currently receives £350k revenue funding from Surrey County Council to support a number of services including recycling, older people's services, environmental services and supporting families. It has been assumed that this funding will disappear over the next 2 years but the services will be maintained at the expense of SHBC.

Fees and Charges

34. The Council generates a significant income from fees and charges, of which £2m alone comes from parking charges. It has been assumed that all charges will increase by 2.00% pa and this has been incorporated in to the forecast.

Property income

35. The Council holds a significant portfolio of investment property which has made a major contribution to the Council's finances.

36. In terms of the SQ it has been assumed that there will be rental growth of only £50k per annum for the forecast period and that £500k of the current temporary rent reductions will be recovered from 2020/21.

37. In terms of rents for other properties, such as the industrial estates, it has been assumed that these will rise by 1% per annum. In addition the forecast assumes that no properties are purchased over the MTFS period however in reality this will be one of the ways that the financial gap will be addressed.

Treasury Management

38. The Council, as at the 30th November 2018, had £14m invested in various institutions and funds. The Council has also taken out a significant amount of borrowing to fund its investments – currently this stands at £140m. The model assumes that this will be at a constant rate of 2% for the life of the forecast or the PWLB rate if already borrowed. In reality the short term rate the Council is using is likely to be less resulting in a significant saving. This advantage will reduce over time as loans have been forward fixed to reduce risk – £25m in 2022 and £25m in 2023 although it has been assumed the average will still be 2%. That said if rates were to rise sharply, each 1% rise would cost £1m pa, then this could put the Council under financial strain.

Capital

39. The Council has an Asset Management Plan and Capital Strategy. The Capital Strategy sets the framework for capital investment and this is supported by the detailed capital programme each year. The Council is currently reviewing its estate to ascertain take advantage of development opportunities and generate returns.

40. The Council has almost no capital receipts and all capital funding is now either from revenue, grants or through internal and external borrowing. It has therefore been assumed that all capital investment will be self-funded.

Level of Reserves and General Fund

41. Local authorities are required, when considering their budget setting, to "*have regard to the level of reserves needed for meeting estimated future expenditure*" and to ensure that the Council has a sound financial position and is able to meet its ongoing and future requirements. It is the responsibility of the Council, together with its Section 151 Officer, to ensure a prudent approach is taken in the administration of financial affairs and that there are sufficient reserves to meet the anticipated demands and requirements of the authority.

42. Reserves generally are kept for 3 overriding reasons:
    - As a working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this forms part of the general reserves
    - A contingency to cushion the impact of unexpected events or emergencies
    - A means of building up funds, often referred to as earmarked reserves, to meet known or anticipated requirements. An example is the ongoing maintenance of a SANG.

43. The main reserve the Council utilises in terms of managing its overall financial position is the General Fund reserve. This reserve is used:

    - To protect the working capital of the authority i.e. to manage fluctuations in spending and to ensure there are sufficient funds to meet the ongoing commitments of the Council;

    - To support the Council through any unforeseen occurrences e.g. to support the Council's budget if there are expenditure pressures such as a loss of car parking income or very high price increases (e.g. in fuel) which are unforeseen

    - To be available to fund emergencies for example flooding etc.

44. As part of its Medium Term Financial Strategy there are also some fundamental principles which apply to how reserves are used:

- The reserves must only be used to fund one off items of expenditure;

- Reserves should be maintained at a sustainable level to ensure an adequate working balance is maintained;

- As the Councils funding becomes more volatile, a higher level of reserves needs to be maintained to manage this volatility.

45. The required level of reserves is not specified by statute, either as a cash amount or as a percentage of the Council's budget. The level set is such that the Council's financial position is maintained, having regard to the risks the authority faces, in the foreseeable future. The Section 151 Officer reports at budget setting time on the adequacy of the reserves and whether they are sufficient for the operation of the Council. Currently the Council holds approximately £27m in earmarked and non-earmarked reserves

46. In assessing the overall level of risk, some of the factors which have been considered are:

- The level of inflation on services and wages;

- The impact of the wider economy on say the housing market and council income and the demand for services;

- The continued reduction in Local Government funding across the country as part of central Government's deficit reduction programme;

- The level of volatility in a number of the Council's income streams such as property and business rates

- Legislative pressures and macro-economic policies such as new responsibilities and changing interest rates.

47. At the moment the level of reserves is considered to be adequate to meet most future risks.

MEDIUM TERM FINANCIAL FORECAST

Introduction

48. The Medium Term Financial Forecast sets out the forecast level of resources and expenditure for the authority over the next four years as at the date of preparation. It is important to note that the figures shown in the plan are local forecasts, based upon a number of local and national assumptions and variables, the majority of which are beyond the control or influence of the Council.

49. In preparing this forecast, the Council has taken into account local and national data regarding resources levels and expenditure pressures. This allows the Council to determine the sustainability of its medium term financial position.

50. Whilst it is highly probable that the figures shown in this forecast will change a key benefit of preparing this plan is to understand the degree to which they could change. This then can enable appropriate actions to be in place to ensure that the Council can deal with such changes.

Revenue Resources Projection

Medium Term Revenue Resources Forecast

51. Using the above individual revenue resource stream projections, the medium term revenue resource forecast is set out below. The forecast reflects an estimate in respect of Local Government funding as far as they are known.

	2020/21 £000	**2021/22 £000**	**2022/23 £000**	**2023/24 £000**
Business Rates	1,250	1,000	750	500
Business Rates surplus	500	0	0	0
Council Tax	8,675	9,052	9,443	9,849
Collection Fund Surplus	200	200	200	200
Special Expenses	185	185	185	185
New Homes bonus	400	400	400	400
	11,210	**10,837**	**10,978**	**11,134**

52. In terms of revenue expenditure, it has been assumed that the cost of services will stay broadly the same, subject to the areas discussed earlier in this paper. In summary the following assumptions have been made around key cost drivers and income streams used in the forecast.

Base Budget Changes				
	2020/21	2021/22	2022/23	2023/24
	£000	£000	£000	£000
Wages Inflation	200	404	612	824
contract Inflation	200	404	612	824
Fees and charges inflation	-140	-283	-428	-577
Rental growth	-40	-80	-121	-162
Interest charges change	-78	-121	-164	-208
SCC Grant reduction	175	350	350	350
SQ rent changes per ME	-50	-100	-150	-200
Hof Rental loss	-500	-500	-500	-500
Total	**-233**	**74**	**210**	**351**

53. The Council has an ambitious capital programme in respect of the SQ and Camberley Town centre. The cost of funding for already approved plans (Phase 1) has been reflected in this forecast. Interest is payable from the date of borrowing whereas MRP, which represents the debt repayment, is only required the year after. An implied interest rate of 2.0% has been used.

54. No allowance has been made for any funding for a new Arena Leisure Centre or the redevelopment of the London Road Site since it has been assumed that these will be self-financing. i.e. The cost of borrowing will be covered by income generated. Were this not to be the case then there could be additional financial pressures or indeed resources.

Revenue Expenditure Forecast

55. Using the assumptions above, the revenue expenditure projection for the authority is shown in the table below.

REVENUE FUND PROJECTION 2019/20 to 2023/24

2019/20 £000 Budget	Portfolio	2020/21 £000	2021/22 £000	2022/23 £000	2023/24 £000
961	Business	961	961	961	961
5,030	Community	4,850	4,850	4,850	4,850
1,852	Corporate	1,745	1,745	1,745	1,745
1,969	Finance	1,969	1,969	1,969	1,969
-480	Town centre and Regeneration	-480	-480	-480	-480
-852	Legal and Property	-852	-852	-852	-852
2,139	Regulatory	2,139	2,139	2,139	2,139
3,421	Transformation	3,421	3,421	3,421	3,421
14,040		13,753	13,753	13,753	13,753
	Other items				
-2,625	Internal Asset charges	-2,625	-2,625	-2,625	-2,625
20	Contribution to Parishes	20	20	20	20
-290	Investment income	-160	-160	-160	-160
2,014	MRP funding - current	2,047	2,098	2,150	2,200
521	Tfr to reserves				
-2,043	Reserves funding	-437	-437	-437	-437
11,637		12,598	12,649	12,701	12,751
	Base budget changes				
	Wages Inflation	200	404	612	824
	contract Inflation	200	404	612	824
	Fees and charges inflation	-140	-283	-428	-577
	Rental growth	-40	-80	-121	-162
	Interest for capital program	-78	-121	-164	-208
	SCC Grant reduction	175	350	350	350
	SQ rent changes	-50	-100	-150	-200
	Hof Rental recovery	-500	-500	-500	-500
0	**Total**	(233)	74	210	351
11,637	**Total Budget to be funded**	**12,365**	**12,723**	**12,911**	**13,102**

Overall Position

56. Using the medium term revenue and expenditure projections, the resulting overall forecast position for the authority is shown below.

Forecast Resources and Expenditure

	2020/21 £000	2021/22 £000	2022/23 £000	2023/24 £000
Resources	11,191	10,790	10,903	11,031
Expenditure	-12,365	-12,723	-12,911	-13,102
Net position	-1,173	-1,933	-2,008	-2,071

57. The gap rises from about £1.2m to almost £2.1m over the life of the forecast driven by reductions in income from property, grants etc. and the impact of inflation.

58. Whilst this can be covered by reserves and indeed the assumptions made may turn out to be better than expected steps will still need to be taken to address this funding gap be it through savings or additional income.

Other issues that may affect the forecast

59. Changes imposed by Central Government could reduce the funding available to Councils and put restrictions on Council Tax. They could also transfer extra duties to Councils, which could have a financial cost, in exchange for greater localisation of business rates.

60. Local factors, such as the pension fund valuation and pressure on wages, could affect the forecast together with more macro-economic factors such as inflation, interest rates and the commercial property market.

Impact of further Capital Expenditure on the forecast

61. So far £6m has been approved for Phase 1 of the SQ refurbishment and about £1m for High Street public realm improvements both of which have been reflected in the forecast.

62. That said, there are further schemes that may be advanced such as Phase 2 at the SQ, capital contributions for the Arena, tenant incentives etc. The revenue cost of this borrowing will depend on the interest rate as well as the length of time the loan is for. Under the prudential regulations the Council must have sufficient revenue resources to cover the interest on the loan as well as make annual provision for debt repayment (Minimum Revenue Payment or MRP). This can add a significant pressure to the revenue budget and ultimately impact services unless it is funded by new income.

63. The table below shows the impact on the revenue budget (interest and debt repayment) of different levels of borrowing over different periods at an interest rate of 3.0%.

Revenue costs of borrowing				
	10 years	20 years	40 years	50 years
	£000	£000	£000	£000
£1m	117	67	43	39
£5m	586	336	216	195
£10m	1,172	672	532	390
£20m	2,344	1,344	1,064	780

Sensitivity

64. The projection can vary widely for a few percentage points. Taking the prudent scenario as a base point then for a number of changes in parameters the savings required for the year ended March 2024 would be:

Change in parameter for forecast period	**Cumulative impact on the forecast**	**Change in projected savings for 2023/24**
No changes – base position	0	2,178
0.5% increase in pay each year	522	2,392
0.5% rise in contract inflation each year	522	2,392
0.5% increase in fees and charges	-366	2,029
0.5% increase in borrowing costs in first year	2,500	2,678
Additional 100 houses for Council Tax	-486	1.930
1% rise in direct rents	-413	2,011
HoF to remain empty for life of forecast	2,000	2,678

65. It can be seen that small variations can have a large impact on the overall projection. Similarly of the Council were to receive a fair share of Business Rates collected – say 5% - then this would add between £0.75m and £1.5m to each year of the forecast.

PROPOSED FINANCIAL STRATEGY

66. The Council's strategy has always been to seek to achieve a balanced budget with no reductions in services to the public. This has required a two pronged approach which firstly looked at increasing efficiency and thus making savings, and secondly at increasing income.

67. The strategy to date has been particularly successful. Over the last 9 years, the Council has reduced its cost base in real terms and yet continued to deliver broadly the same range of services without any impact on the public at large. Initially this was achieved through changes to staffing, greater use of technology and collaborative working with other public bodies. However as the scope for further savings reduced, the emphasis changed to one of income generation through the introduction of new chargeable services, increasing existing charges, getting better returns from assets and investing in property for growth. This income growth, particularly from property whether bought for investment or regeneration, has made a major contribution to the Council's finances and enabled it to deal so far with the financial challenges placed upon it by Central Government. However this success has been at the price of the Council taking on increased risk, as can be seen by the recent downturn in retail property, and so the challenge for the Council is not only about generating more income but also coping with the volatility that this can sometimes bring.

68. There are a number of different areas the Council should concentrate on in order to address its financial challenges going forward. These are as follows:

Business Rates and Needs based funding

69. A key area of uncertainty is the Government position on the full localisation of Business Rates and Needs Based Funding. Currently Surrey Heath gets to keep less than 4% of the Business Rates it collects and this may reduce even further over time. There is no way this could be described as "an incentive for growth" and so the Council needs to continue to lobby to ensure it gets a fair share of the economic growth it creates.

Continue to lobby the Government to give a fairer deal to Districts by fixing the baseline at the actual rates achieved and to provide within the new localisation scheme a genuine incentive for growth.

Delivery of Housing

70. The delivery of housing within the Borough is a key driver for economic growth and is in line with Government policy. An additional 1,000 houses over and above the baseline of 149 units would not only give an additional £212k in Council Tax *per year* but also potentially £4.8m in New Homes Bonus. Affordable Housing not only attracts a higher NHB but also reduces the cost of bed and breakfast and homelessness within the borough.

Support the delivery of significant new housing developments within the Borough.

Internal efficiency

71. Whilst a lot of work has already been done to release the easier efficiencies, there is still scope for further work to be done in areas such as shared services, combined management, better procurement, reduced customer contact and streamlined management.

Internal efficiencies, including demand management, and collaborative working, including reducing the number of Surrey Councils, be pursued to deliver further efficiencies

Additional income from charges

72. Charging for discretionary services is an accepted way of increasing resource to support other areas of the Council's activities. For example, charging for parking in parks, where in effect the user pays for the discretionary service they are using.

Introduce new charges in order to generate income to support unfunded services

Additional income from assets

73. The Council has been successful in renting space to partners in Surrey Heath House. So far this contributes £250k to the budget in terms of rent and shared service costs. Applying agile working to all Council staff would free up more space for rent and deliver more income. There is also potential to generate capital receipts from the development of surplus land across the borough and use this to reduce debt.

Put in place a new asset management strategy which will seek to rent out surplus office space and develop/sell surplus land

Reduction in provision of Discretionary Services

74. The Council provides a whole range of services which are not required by statute and therefore not funded. This includes Meals on Home and Community Buses, the theatre, parks and the museum. These services in total cost around £1m hence steps have been taken over recent years to reduce their cost. These services may need to operate on the basis of "the user pays" or be reduced over time. Services which are the legal responsibility SCC may need to be handed back if SCC is unable to adequately fund them.

Work to reduce subsidy for Discretionary services and discuss with Surrey how funding for these services can be maintained

Generate Income through Investment

75. Surrey Heath has invested heavily over the past few years and this made a significant impact on its budget position in 2017/18. Although 2018/19 has proved to be difficult in terms of retail rents it is worth stating that the Camberley Town Centre was never purchased as a pure investment but rather to kick start regeneration and maintain the local economy. That said it still makes a hefty contribution to the finances. Despite the risks investment in property is likely to be the only thing which can bridge the financial gap the Council is forecasting in the time available.

76. The Council has always been open about the risks from property investment. It has sought to reduce these risks by using professional advisers, concentrating on the local market, having a mixed portfolio and looking for solid investments. Of the Council's current investments about 25% are in industrial property with the remainder in retail. It was always intended that property purchased would be held for the longer term with a focus on maintaining income rather than capital growth. As income becomes more volatile, it will be essential that the Council maintains adequate reserves to enable it to deal with these peaks and troughs as they occur.

77. It is important that income from existing investments is maximised. This is because the loan has to continue to be financed even if the income from the asset is much reduced. It is therefore vital that property when it becomes empty is either re-let or repurposed as quickly as possible so as to minimize the adverse impact on the Council's finances.

Continue to invest prudently in property to generate additional income and ensure that income from assets already owned is maximised

78. The strategy above has already been shown to work, and despite some fluctuations, has enabled the Council to maintain services despite losing a significant amount of Government funding.

Looking ahead

79. It is clear that the Council will continue to find itself in an environment where the need to deliver savings and income growth is ongoing. This is due in the main to the Government taking more and more of the Councils resources, as well as the fact that rising cost and demand far outstrips the ability of Council Tax to fund them. Unless the Government is prepared to share to business rates more fairly only a strategic re-organisation of Local Government in Surrey can eventually deliver the financial cost savings required. In the meantime continued investment, development and more efficient working will be needed to plug the gap.

80. The performance of the wider economy could have a significant impact on the Council's finances in the years to come which will need to be managed.

RISK MANAGEMENT

81. The Corporate Risk Register includes the risk of the Council being unable to deliver a balanced financial strategy over the medium term. Specific risk factors include:

    - External limitations including the Government's ongoing review of Local Government resources, planned localisation of Business Rates and Council Tax pressures including capping;

    - Reduced income from fees and charges, which the Council is dependent upon to help balance its revenue budget;

    - Budget pressures created by change in demand – decrease/increase in demand for existing services or demand for new services and increased customer expectations.

    - In respect of Business Rates, were the claim for charitable relief from NHS bodies be successful the Council would have to repay up to £6m and potentially lose £500k pa in income depending on how the localisation works.

    - Risks inherent in property investment and development in terms of movement in the market, development overruns and loss of sales, rental void periods and competition. This risk, driven by the national economy particular in respect of retail, is by far the most significant risk the Council faces and could prove to be very difficult to manage.

    - Risks arising from interest rate changes. The forecast is based on an average rate of 2% and at the moment the council is achieving significantly below this. However if this was to change by 1% then this could potentially add £1m to interest rate costs. This risk has been partly reduced by taking a forward loan for £50m at a fixed rate.

82. The Council is attempting to address these risks by ongoing sound financial management and placing an emphasis on value for money, efficiency planning and invest to save initiatives. The Council conducts a thorough due diligence process on all its investments and employs professional advisers to advise it on potential acquisitions to try to minimise risks.

83. The Council also employs professional property managers to advise on tenants and maintain income from the estate. The quality of this advice will be crucial in the very difficult times ahead. Whilst not investing in property would eliminate the risk, it would lead to a reduction in services to cover the loss in funding the Council has suffered.

84. The Council seeks to manage its risks, at least in the short term, by retaining an adequate level of reserves to allow time for other actions to be taken.

85. A major risk, which is outside of the Council's control, is the financial stability of Surrey County Council. In the forecast it has been assumed that Surrey CC funding will be withdrawn over 4 years. Were this to happen more quickly this would increase the financial pressure on Surrey Heath as it tries to maintain those services. In addition Surrey CC has an ambitious savings program which needs to delivered if it is to remain financially viable. If it was unable to achieve this then this could lead to a full reorganisation of local government within Surrey as has happened in Northamptonshire. Were this to happen any financial obligations entered in to by Surrey Heath would transfer to the new Council.

EQUALITIES

86. The strategy has been prepared as far as possible in line with the Council's approach to equalities in that it does not discriminate or support discrimination on the grounds of age, disability, gender, race, religion or belief, or sexuality. The effect on protected groups of actions required to deliver the strategy would form part of an Equalities impact assessment when those changes are considered

OVERALL CONCLUSIONS

87. This strategy and forecast give an overview of the current and future position of the Council. Prospects for the Borough's finances are better than they might have been due to the focus on income generation, but the financial challenges continue to grow in the years ahead.

88. Maintaining reserves does enable the Council to cover cyclical shortfalls in income for a few years until rents recover in the future. However, despite the current issues around retail investment, the Council has taken the decision to invest in its own town centre to deliver regeneration and hence it must continue to support these through investment with the view that there will be a positive outcome. The Council can take some comfort that its track record so far has been good. Savings have been achieved, income generated and most importantly services maintained, however the challenge continues. Work will need to continue in earnest to seek more efficiencies and to generate income through construction lead growth, new charges, asset utilisation and investment. This will also include giving up some control in order to work more closely with other local authorities.

89. Whilst the last few years have brought challenges to Councils, they have also given real opportunities to those that are prepared to take the initiative. Surrey Heath has shown through its investment in property and transformational approach to services that it is not afraid to take difficult decisions. The course has been set and the journey started – now we just have to "Keep calm and carry on".