HAMPSHIRE COUNTY COUNCIL

Decision Report

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Date:	6 February 2015
Decision Maker:	Council
Date:	19 February 2015
Title:	Revenue Budget and Precept 2015/16
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Report From:	Director of Corporate Resources

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1. Executive Summary

1.1. The purpose of this report is to set out the County Council's proposals for the revenue budget and precept for 2015/16. It incorporates decisions on savings proposals made as part of last years budget setting process and which are currently being implemented as part of the Transforming the Council to 2015 programme.

1.2. The report recommends a further freeze in the council tax level, meaning it will now have been at the same level for the sixth year running. Government grant equivalent to a 1% increase (£5.475m) will be paid to compensate for the lost income as in previous years.

1.3. The Transforming the Council to 2015 Programme will achieve savings of £102.5m which have been incorporated into the budgets detailed in this report. These savings, together with additional one off income from council tax collection and business rates retention mean that a balanced budget can be set for 2015/16 without the need to draw from the Grant Equalisation Reserve.

1.4. Financial performance in the current year remains strong, with the main pressure, as in previous years, being around the increasing demand for Adult and in particular Children's social care. Both Departments have action plans in place to contain this pressure in the current year and this report recommends a base budget increase for Children's Services of £12.5m for the increasing costs of Children Looked After in line with the projections set out in the Medium Term Financial Strategy.

1.5. During January individual Executive Members have been considering their revenue budget proposals with the Leader and Cabinet and this report consolidates these proposals together with other items that make up the total revenue budget for the County Council in order to recommend a budget, precept and council tax to full County Council on 19 February 2015.

1.6. It should be noted that the figures in this report in respect of government grant levels and figures notified to the County Council by District Council's are provisional at this stage and will be subject to change. Revised figures will therefore be presented to full County Council and this report seeks delegated authority for the Director of Corporate Resources in consultation with the Leader and Chief Executive to make these changes as appropriate.

2. Background

2.1. Members will be fully aware that the County Council has been responding to reductions in government Grant since the first reductions were applied in 2010/11 and then as part of the Comprehensive Spending Review (CSR) 2010.

2.2. It was thought at this stage that the period of austerity would last until the end of that CSR period (2014/15) and consequently the County Council planned and implemented four years worth of savings in two years totalling £100m.

2.3. By 2013, it was clear that the period of austerity would extend beyond this at least to 2017/18 and work was therefore started on Transforming the Council to 2015, to deliver a further £102.5m of savings by April 2015. This was based on an assumption of a 10% reduction in all Government grant streams, which for 2015/16 equated to £27.1m.

2.4. The final grant settlement for 2015/16 is not due out until this report has been dispatched, however based on the provisional figures released in December last year, this confirmed that the County Council will have a further reduction in grant of 11.8% equivalent to around £30m and £2.9m higher than had been forecast.

2.5. This does however take account of the fact that council tax freeze grant from 2014/15 has been 'baselined' into Revenue Support Grant in line with the Governments announcement last year. This remains a significant risk to the County Council going forward since the Medium Term financial strategy assumes that all past Council Tax freeze amounts will be built into baseline grant from 2016/17 onwards.

2.6. The Chancellor also announced last year that a further grant would be available in 2015/16 to those authorities that agreed to freeze the council tax for a further year, equivalent to the income from a 1% council tax increase, estimated at £5.475m for the County Council.

2.7. In December last year Cabinet received a budget update report that set provisional cash limit guidelines for Departments, taking into account savings targets, inflation and base changes. This report confirms the cash limits that will be applied to Departments next year and after allowing for additional allocations to pay for the agreed pay award the individual reports approved by Executive Members during January all show (with the exception of Children's Services, the reasons for which are explained in this report) that the proposed budgets are within the cash limit guidelines that have been set.

3. Third Quarter Budget Monitoring

3.1. The third quarter monitoring position remains largely unchanged from the half year position and reflects the strong financial management grip across the County Council. Most Departments are expecting underspends resulting from early delivery of savings during the year.

3.2. Adults and Children's Services are both expected to be at a break even position by year end through pro-active management of the services together with the use of Departmental reserves and agreed corporate support.

3.3. Pressures in the acute sector are still a concern in terms of the knock on impact on adult services and this has been recognised by the Government through additional grant of £520,000 for the County Council.

3.4. The next section outlines the expected outturn position for the current year in more detail.

4. Revised Budget 2014/15

4.1. During the current financial year there have been a number of changes to the original budget that need to be taken into account, some of which have been reported to Cabinet through the quarterly budget monitoring reports. In addition, it is also timely to review some of the high-level numbers contained within the revenue budget in order to assess the likely impact on the outturn position for the end of this year.

4.2. Appendix 1 provides a summary of the original budget that was set for 2014/15 together with adjustments that have been made during the year. The proposed Revised Budget for 2014/15 is then set out for information. The variance between the adjusted and revised budget gives an indication of any one off resources that may be available at the end of the year that could be used to provide additional contributions to the Grant Equalisation Reserve.

4.3. The paragraphs below explain the main adjustments that have been made to the budget during the year:

4.4. **Departmental Spending** – Departmental spending has increased by £25.7m, the reasons for this are highlighted in the table below:

	£M
Change in Dedicated Schools Grant	0.9
New grant for Free School Meals	9.3
New grant for SEN reform & implementation	2.4
New grant for Bus Service Operators	1.1
Net increases in other specific grants	2.0
Adult Services – transitional costs of the extra care	2.1
Use of cost of change reserves	2.5
Impact of pay award	2.2
Use of grants carried forward from 2013/14	1.8
Other Net Changes	1.4
Total	25.7

4.5. **Pension Costs -** Pension costs for past deficit payments are now accounted for centrally. The increase of £1.2m reflects the agreed recovery plan for the latest actuarial valuation of the fund which will increase by 8% per annum for the next five years.

4.6. **Revenue Contributions to Capital Outlay (RCCO)** – The increase in RCCO reflects changes made to the capital programme and financing made during the year but this is entirely offset by other funding changes in budgets or to earmarked reserves so that there is no bottom line impact in 2014/15.

4.7. **Contingencies** – the reduction in contingencies is the result of transfers made to Departmental budgets during the year.

4.8. **DSG and Specific Grants** – The increase in DSG reflects minor amendments that have been made to the final grant during the year. The increase in specific grants is mainly due to the receipt of £9.3m in respect of the universal provision of free school meals.

4.9. All of these changes have had a minimal impact on the bottom line of the revenue account as they mainly represent transfers between different areas of the budget or represent matching additions of expenditure and income as is the case with additional specific grants.

Revised Budget 2014/15

4.10. The fourth column of figures shown in Appendix 1 outlines the proposals for the revised revenue budget for the County Council for 2014/15. At this stage the revised budget for Departments matches the adjusted cash limits that they have been given for the year and therefore no variances are shown for the end of the year. As part of the quarterly monitoring reports presented to Cabinet it is anticipated that there will be under spends in Departmental budgets by the end of the year, however in line with current policy all of these underspends can be transferred to Departmental earmarked reserves to be used to fund the cost of change in future years and therefore would still have no impact on the bottom-line position of the revenue account.

4.11. The forecast position for the majority of services is break even against the revised cash limits reflecting the fact that most Departments are managing their bottom line positions to contain spending pressures or are using any surplus to meet the cost of change in the year instead of drawing from reserves.

4.12. **Interest on Balances -** The County Council adopts a prudent approach to estimating for interest on balances given the number of different variables involved. For 2014/15 the budget was increased by £5m (to £5.75m) to take account of historic levels of investment returns and to reflect a change in the investment strategy to look at higher yielding medium term investments. Current forecasts anticipate that performance in the year will exceed this figure and an additional return of £650,000 is therefore assumed in the revised budget.

4.13. **Capital Financing Costs** – As in previous years, the estimates for this heading are prepared on the basis of taking out new planned borrowing during the year. However, since the County Council has significant cash reserves there is no need to actually take out this long term borrowing at this stage particularly since this would attract a high 'cost of carry' when comparing short term to longer term interest rate levels. The estimates for 2014/15 have therefore been revised taking this factor into account and show a saving of £3.75m in the overall capital financing costs for the year.

4.14. **Contingencies** – The key items within this budget relate to risk contingencies set aside to reflect the major change and savings programmes that were being embarked on during the year, allowance for waste disposal inflation and disposal costs, together with some other centrally held contingencies in respect of pay and price increases.

4.15. In considering the Revised estimates position, it is timely to review these contingencies in light of the current financial position highlighted in monitoring reports. At this stage of the year, it is considered prudent to release contingency items in respect of pay and price inflation which have not been used, together with other sums set aside for income risk and the general risk contingency. In total, these items amount to £7.2 million which can be declared as savings against the revised budget.

4.16. Taking this £7.2 million, together with the £4.4m available from capital financing and interest on balances gives a grand total of £11.6m that can be used on a one-off basis to help replenish the Grant Equalisation Reserve.

4.17. It is important to note that whilst these do represent significant available resources, they must be set in the context of the size and complexity of the County Council's gross budget and the efficiency and change programme that has been implemented in recent years. Contingency sums are set aside for a variety of purposes and it is only now at this late stage in the year that these resources can be deployed for other purposes with greater certainty.

5. Local Government Finance Settlement

5.1. The final Local Government finance settlement for 2015/16 is still awaited at the time of the publication of this report. Overall, the provisional settlement has reduced the County Council's Revenue Support Grant by £25m. However this sum also includes the 'baselining' of council tax freeze grant from 2014/15, which means the adjusted reduction is around £30m and equates to an 11.8% reduction on total grants (as measured by the Start Up Funding Assessment), which is £2.9m worse than the assumption in the budget forecast.

5.2. The provisional settlement also contains continuation of the compensation for lost business rate income, following the previous announcements on caps and reliefs which will be paid in a separate grant.

5.3. The Chancellor had also announced that there was to be a fifth year of council tax freeze grant to be made available, equivalent to a 1% increase in council tax (£5.475m). This grant will be payable for 2015/16 and is then expected to be baselined in line with the Government's announcement last year.

5.4. Other changes included a reduction in Education Services Grant of £684,000 and the discontinuation of the Local Welfare Provision Grant of £1.573m which in line with the current 'passporting' policy for specific grants means that expenditure on this service will cease. However, past unspent Local Welfare Provision funding of around £1.2m will be carried forward at the end of this year to provide transitional funding to support the managed reduction of this service over the next two years.

5.5. The overall reductions outlined in this section and the impact on the budget for 2015/16 are set out in Section 10.

6. Service Cash Limits 2015/16

6.1. In December 2014 Cabinet considered a budget update report which set provisional cash limit guidelines for Departments for 2015/16. Appendix 2 sets out those cash limits and provides information on adjustments that have been made since this time. Overall, cash limits have increased by £55.2 million, some of the reasons for which have been outlined in the individual budget reports to Executive Members. The reasons for the increase are shown in the table below:

	£M
Increase in Children Looked After base budget	12.5
Impact of pay award	5.9
Increase in Public Health grant for 0-5 year old provision	8.8
Increase in Dedicated Schools Grant	10.2
Increase in Universal Free School Meals grant	6.6
New Burdens Funding for impact of Care Act	7.6
Increase for Children's Services following consultation	2.8
Other net changes	0.8
Total	**55.2**

6.2. In a similar way to the changes for 2014/15 only some of these amendments have a bottom-line impact on the revenue budget as they represent transfers between Departments or as a result of changes in grants, contingencies, earmarked reserves or RCCO.

6.3. Following the December Cabinet meeting, further work has been undertaken to confirm as best we are able, the impact of the increasing numbers and complexity of Children Looked After. Based on current forecasts it is still anticipated that a base budget adjustment (covering the anticipated growth across two years) of £12.5m is required in 2015/16 and this has been added as part of this report. However, given the volatility in this area, this together with increases in growth in Adult social care remain a key risk in the budget that will need to be taken into account in setting the level of contingencies.

6.4. The other key change relates to additional cash limits that have been given to Departments for the impact of a two year pay deal which is payable from January 2015. For most grades this equates to a 2.2% increase but there are also higher increases for lower paid staff which has increased the overall cost of the pay award to around 2.4%. This is higher than had been allowed for within the forecast but has been met from the overall inflation amounts contained within the budget, so has no bottom line impact.

6.5. The £2.8m proposed increase for Children's Services in respect of changes arising from consultation is outlined in more detail in the next section.

7. Savings Proposals

7.1. The County Council has been working for some time now on the Transformation to 2015 Programme, which aims to deliver £102.5m of savings as part of the 2015/16 Budget. Given the size of the task, the lead in time required and the transformational nature of some of the proposals, the detailed savings proposals to meet this target were approved in February 2014 as part of the budget setting process for 2014/15. There are therefore no new savings proposals to consider as part of the formal budget setting for 2015/16, but the impact of the agreed savings has been reflected in the detailed budgets approved by Executive Members and presented in this report.

7.2. During 2014/15, Departments have been implementing these proposals, carrying out specific consultation exercises where these were required and Executive Members have taken further decisions on the final detailed proposals where this has been necessary. There are two particular consultations that need to be considered in this report following a request from the Executive Lead Member for Children's Services to increase the 2015/16 cash limit on a one-off basis for the Children's Services Department by £2.8m.

7.3. Savings proposals in respect of Short Breaks for Children with Disabilities and Commissioning of Youth Support Services were approved as part of the Transformation to 2015 Programme agreed by the County Council as part of the budget setting process last year.

7.4. The purpose of agreeing savings proposals well in advance of the financial year to which they related was to give the time and capacity to properly implement the changes, which in some cases, due to the nature of the proposals, meant carrying out specific consultation exercises before final decisions could be made on service changes.

7.5. Consultation exercises on these two proposals were therefore launched in September 2014 for Short Breaks and October 2014 for Youth Support Services, with a view to reporting the outcomes to the January meeting of the Executive Lead Member for Children's Services.

7.6. In the finance update report to Cabinet on 15 December 2014 acknowledgement was given to the fact that the implementation of some proposals would be more challenging than others and were subject to separate consultation exercises to fully understand the impacts of the proposals. It was stressed that taking the time to get this right was very important for service users and the County Council and as such some savings might not be achieved in 2015/16 and might therefore need to be supported on a one off basis, generally from Departments' cost of change reserves.

7.7. Specific reference was made to the proposals for Short Breaks and Youth Support Services in this regard and the impact that this may have on the ability to make savings in 2015/16. Given this position it was agreed that corporate cash flow support would be provided on an exceptional basis in the next financial year due to the fact that Children's Services cost of change reserves were likely to be depleted given the requirement for them to fund £6.3m of Children Looked After pressures in the current year.

7.8. The consultation exercises for both of these proposals closed in December 2014. The County Council, in carrying out consultations of this sort recognises that proposals to reduce levels of provision in any service are not going to be popular and that consultation responses will inevitably reflect this. However, the purpose of consultation is also to listen to key service users and other interested parties and to ensure that final decisions made by the County Council fully take this feedback into account.

7.9. It is also important to remember that the original decision to pursue these proposals was made by the County Council nearly a year ago and since that time more information has become available about the changes being implemented across the Council as part of the Transformation to 2015 Programme together with initial considerations arising from the Opportunity Assessments being carried out to support the Transformation to 2017 Programme.

7.10. Senior Managers in consultation with the Executive Lead Member for Children's Services have reviewed all the comments made within the two consultations and given them careful consideration. In the light of the points made during these consultations and the wider context of the Transformation 2017 Programmes across the Council, it is considered appropriate at this stage not to implement either of the savings in their current form as part of this 2015/16 budget setting process.

7.11. Early considerations of the further savings that will be needed by April 2017 suggest that the shape and delivery of services for Children with Disabilities and Youth Services will need to undergo further transformation alongside all children's services. The Lead Executive Member therefore recommended that Cabinet formally approve one off support of £2.8m for Children's Services in 2015/16 as part of the budget setting process to allow further time to consider the future shape of these services. This report recommends that Cabinet agree this change given the feedback arising from the consultation exercises, and the figures in the rest of the report assume that this will be approved.

7.12. Going forward potential savings in respect of services to Children with Disabilities will be picked up in the wider context of the Transformation to 2017 Programme. This means that Short Breaks for Children with Disabilities will be maintained in their current form at current funding for the financial year 2015/16.

7.13. For Youth Support Services the total financial envelope will be unchanged for the 2015/16 financial year. Delegated authority was given to the Director of Children's Services to approve grants for youth services as appropriate up to the maximum values to any one organisation as previously granted by the Executive Lead Member for Children's Services for the 2014/15 financial year. As part of this exercise the Director will continue the discussions that commenced during the consultation exercise to look at future service delivery options, and build on work already undertaken.

7.14. Further one-off corporate cash flow support for either of these proposals beyond 2015/16 will be considered in light of the next stages of the processes set out above, but will be on the basis of repayment by Children's Services as outlined in the December 2014 Cabinet report.

Transformation to 2015 Progress Reporting

7.15. Progress on the implementation of the Transformation to 2015 Programme is reported to Corporate Management Team (CMT) every month and is formally reported on to Cabinet. Two internal peer review processes have been carried out to ensure the Programme is on track and the second of these forecast that a minimum of £96.4m of the total savings requirement would be delivered in 2015/16.

7.16. The Chief Executive has requested the Director of Corporate Resources to put in place enhanced monitoring of the Transformation to 2015 Programme as we move towards the beginning of the financial year and this will be included within a financial dashboard that will be reported and scrutinised by CMT on a monthly basis. A key focus as ever will be that we maintain strong financial management during the year to ensure that all Departments stay within their cash limits, that no new revenue pressures are created and that they deliver the savings programmes that have been approved.

8. Service Budgets 2015/16

8.1. As explained in Section 6 Departments have been set cash limit guidelines for 2015/16 which include allowances for inflation, base changes and the savings targets set for each Department.

8.2. Appendix 3 provides a summary for each Department of the main services under their control and shows the original budget for 2014/15, the revised budget for 2014/15 and the proposed budget for 2015/16. All Departments are proposing budgets that are within their cash limits, after taking into account the proposed increase in Children's Services cash limit as explained above.

8.3. Fees and charges have been raised where there is scope to do so in policy and economic terms, and the inflation allocation has been calculated on the basis that charges are increased in line with the allowance for inflation on expenditure, taking into account areas where it is not necessarily possible to increase charges due to the nature of the arrangements with the clients that we do business with (for example where a fixed income contribution has been agreed in the past). Details of income reviews and charges were set out and approved in the budget reports for Executive Members.

9. Workforce Implications

9.1. The County Council has from the outset been managing the reduction in the workforce in response to the reductions in Government Grant in a planned and controlled way by the use of a recruitment freeze, redeployment of staff where possible and a successful voluntary redundancy scheme, which has been used to effectively and sensitively manage staff reductions at what is a very difficult time.

9.2. In preparation for the Transformation to 2017 Programme a final offer of Enhanced Voluntary Redundancy (EVR) has been made to all non-schools staff in the County Council. Decisions on these are expected to be made by the end of this financial year, but the leaving dates for staff that are accepted will extend into 2016 in order to effectively manage the reduction in the workforce.

9.3. Assumptions around staff reductions as a result of the current EVR process have not been included within the figures within this report, but given the current financial position and the fact that this is the last enhanced offer of voluntary redundancy, it is anticipated that the numbers could be significant.

9.4. It is important that this EVR programme is a success as it will create a strong platform and provide early momentum for the Transformation to 2017 Programme. This early momentum is also particularly important as we move into the 2015/16 financial year and we focus on the need to maintain financial prudence across the County Council to provide a strong base position for the budget for 2016/17 and beyond.

9.5. Decisions on EVR applications are considered on a case by case basis by Directors against specific criteria, in addition, the payback period of letting someone go is also an important consideration.

9.6. Given the financial imperative of the EVR programme outlined in paragraph 9.4 and the profile of the likely applicants for EVR it is felt that an average payback period of up to around 18 months across Departments can be expected, although each individual decision must be considered on its own merits and take into account personal circumstances.

9.7. Appendix 4 provides a summary of the workforce changes that are expected to happen by the end of 2015/16 and take account not only of the anticipated reduction in posts as a result of the ongoing implementation of savings proposals but also other changes and transfers that have or will impact on Departments during the year. A high-level explanation of the main changes within the Departments is also provided within the Appendix.

9.8. The net change in posts is an increase of 219, which reflects the fact that whilst in some areas the number of roles is reducing and changing, in others, we are expanding business either through partnership working or through the extension of trading activities as is the case with Property Services and our catering service HC3S. This reflects the County Council's innovative and diverse approach to tackling the financial challenges that it has and continues to face.

10. 2015/16 Overall Budget Proposals

10.1. Whilst service budgets make up the vast majority of the total budget there are several other items that need to be taken into account before the overall budget and council tax can be set for the year.

10.2. Appendix 5 sets out a summary of the overall revenue account starting with the cash limited expenditure for Departments that have been discussed above. The following paragraphs outline the other items that make up the overall revenue account and provide explanations for any significant variances compared to the 2014/15 budget.

10.3. **Interest on Balances and Capital Financing Costs** – The reduction of just under £2.5m is made up of increased investment income of £1.5m which reflects the ongoing impact of the revised investment strategy agreed in February last year together with reductions in capital financing costs of just under £1m that reflect a lower level of actual long term borrowing than anticipated and reduced interest payments for PFI contracts.

10.4. **Pension Costs** – Pension costs for past deficit payments are now accounted for centrally. The increase of £2.1m reflects the agreed recovery plan for the latest actuarial valuation of the fund which will increase by 8% per annum for the next five years.

10.5. **Revenue Contributions to Capital Outlay (RCCO) -** Each year, revenue contributions are made to help fund the capital programme. The significant decrease of nearly £13m is almost entirely due to the change in the amount of RCCO drawn from reserves, which is offset by an equal amount in the reserves section of the revenue account and therefore has no impact on the overall budget.

10.6. **Contingencies -** The budget for contingencies has increased by around £11.8m over the 2014/15 original budget and reflects a re-assessment of contingencies to deal with the revised approach to social care growth agreed as part of the Medium Term Financial Strategy.

10.7. Existing contingency provisions in respect of key risk items such as Extra-Care transition costs and income risks have been retained in the base budget and these provisions represent the recommendation by the Director of Corporate Resources of a prudent approach to budgeting given the potential pressures the County Council faces. In addition to these contingencies, the County Council has access to significant reserves as part of an on-going strategy to for the management of the County Council's financial resources over the medium term.

10.8. **Dedicated Schools Grant** - The increase in this budget is due to the increase in pupil numbers and the carry forward of 2014/15 funding.

10.9. **Specific Grants** - This income budget has increased by £30.5m, mainly as a result of the increased grant provided for universal free school meals (£15.9m), the part year impact of the transfer of 0 to 5 year old public health provision (£8.8m) and the provision of new burdens funding for the impact of the Care Act (£7.6m) This has been partially offset by a reduction in a number of other grants within Children Services, which had been provided for 2014/15 only and the discontinuation of the Local Welfare Provision grant.

10.10. **Council Tax Freeze Grant** – Although it appears that there has only been a small movement in this grant budget, this masks the fact that £5.3 million received for the 2014/15 council tax freeze has now moved directly into formula grant, but has been replaced by additional grant of slightly more than this arising from the recommendation to County Council in this report that council tax be frozen for 2015/16.

10.11. **Coroners Service** – Although the Coroners Service is reported as part of the Policy and Resources budget, it does not form part of the cash limit, as the County Council has no control over the level of spending within this service. It is therefore shown as part of the overall revenue account and it is anticipated that based on recent years spending patterns that the funding will remain the same for 2015/16, although this incorporates additional costs of coroners officers that have been transferred from Hampshire Constabulary offset by efficiencies made within the service over the last 12 months. Actual spending is of course dependent on the number of cases arising during the year and any spend in excess of this amount will be met from contingencies.

10.12. **Earmarked Reserves** - Changes to earmarked reserves mainly reflect changes to other budgets elsewhere in the revenue account. However, the significant reduction in the draw from earmarked reserves in 2015/16 reflects the fall out of the use of the Grant Equalisation Reserve to balance the budget in 2014/15. As explained later in the next section, no draw from the Grant Equalisation Reserve is required to balance the budget for 2015/16.

10.13. The County Council holds reserves for many different reasons, but not all of these are available for general usage, schools balances are for schools exclusive use and other reserves such as the insurance reserve are set aside as part of the Council's overall risk management strategy or are already planned to be used as is the case with the grant equalisation reserve which is utilised over a number of years in order to dampen the impact of grant reductions and to provide the time and capacity to develop savings for implementation.

10.14. A comprehensive Reserves Strategy was presented as part of previous MTFS updates to Cabinet and Council and this has been updated to include the figures at the end of March 2014 and is set out in Appendix 6.

10.15. This highlights the point that only 16.9% of reserves are truly available to be used to support revenue spending and to help fund the cost of the change programmes across the County Council. Of the £50.5m shown for the Grant Equalisation Reserve £28.5m is budgeted to be drawn to balance the budget in

2014/15 and the corporate efficiency reserve will be utilised to support the Transformation to 2017 Programme.

10.16. **Use of General Balances** –The 2014/15 budget assumed a net draw from general balances of £7.1 million, representing the use of unspent contingencies carried forward from 2012/13 in order to provide adequate contingency levels within the budget up until the 2014/15 financial year. The adjustment of £8m returns the budget to a contribution to general reserves of £900,000 per annum to maintain the minimum level of reserves at an appropriate level as recommended by the Director of Corporate Resources, currently around £21.5m.

10.17. Appendix 7 represents the Director of Corporate Resources view of the overall budget and the adequacy of reserves which must be reported on as part of the main budget proposals in accordance with Section 25 of the Local Government Act 2003. In particular, it considers risks within the budget and in the MTFS going forward and sets this in the context of the recommended contingencies and balances set out in this report.

11. Budget and Council Tax Requirement 2015/16

11.1. Although this report recommends taking the council tax freeze grant for 2015/16, there are still other changes within the council tax calculation that can have an impact on the budget. The County Council is notified by Hampshire Districts, of the estimated level of collection fund surplus or deficits that needs to be taken into account in setting the council tax for 2015/16. In addition to the figures for council tax, Districts are required to provide estimates of their surplus or deficit on the Business Rates collection fund, following the introduction of Business Rates Retention in April 2014.

11.2. For 2015/16 a net council tax collection fund surplus of just over £9.9m is anticipated which is £8.4m above the level assumed in the original forecast for the year. This has mainly arisen due to general increases in the council tax base during the year, but also as a result of continued changes in local Council Tax Support Schemes (CTSS) which replaced council tax benefit from April 2014. The impact of these schemes was difficult to predict in terms of changes in council tax base and collection rates and indications are that the reductions are not as great as originally anticipated.

11.3. The current prediction for business rate collection funds is a £924,000 surplus across all Districts, although there are varying levels of surpluses and deficits that make this up. This reflects the fact that the position is settling down after the first year of operation which saw significant complications and losses around the treatment of past and potential future appeals. There is however still some volatility in this area and this could therefore be subject to change after this report has been despatched.

11.4. Similarly, Districts have provided estimates of what Business Rate income they expect to receive for 2015/16, based on their experience during the current financial year. Latest estimates show that income will be around £2.0m higher than was assumed in the budget forecast for next year. This includes some significant increases within some District Councils that could be as a result of the large provisions for appeals that have been made in the early years of the rates retention scheme. However, these figures have been queried back with the individual authorities, given the scale of the increases and this therefore remains a high risk area within the current budget figures which may have to be adjusted at County Council.

11.5. Final details of the compensation grant that Hampshire is due to receive following the caps and reliefs granted by Government in past budgets have yet to be notified and will therefore change the anticipated income from this source in the final budget.

11.6. In addition, paragraph 5.1 outlined the fact that following the provisional settlement in December last year, the County Council has received a further reduction in Revenue Support Grant of £2.9m, which feeds into the overall Council Tax calculation.

11.7. The financial update report presented to Cabinet in December 2014, forecast that £5.6m would need to be drawn from the Grant Equalisation Reserve to balance the budget in 2015/16. Taking into account the proposed increase in Children's Services cash limit and all of the items in this section, gives the following position:

	£'000
Draw from balances assumed in MTFS	5.6
Further loss of Revenue Support Grant	2.9
One Off Cash Limit increase for Children's Services	2.8
Business rates collection fund surplus	(0.9)
Business rates ongoing revenue increase	(2.0)
Additional council tax collection fund surplus	(8.4)
Balanced Budget	**0.0**

11.8. The table above shows that as a result of the one off surpluses in council tax and business rates, the County Council is able to set a balanced budget without the need to draw from the Grant Equalisation Reserve. This provides more funding to help tackle the future challenges that are still to come, however given the one off nature of the funding it does not change the provisional savings requirement of £98m already set for 2017/18.

11.9. Local authorities are required to report a formal council tax requirement as part of the budget setting process and the recommendations to Council later in this report show that the Council Tax Requirement for the year is £504,890,644.

12. Treasury Management Strategy and Investment Strategy for 2015/16

12.1. The County Council is required to adopt a treasury management strategy and an annual investment strategy for 2015/16 and these are set out in Appendix 8 for approval. The strategy has been reviewed in light of the continuing turmoil in the world economy and the borrowing strategy reflects the intention of taking a more active approach to managing the portfolio of existing borrowing.

12.2. As previously outlined the revised approach of placing a part of the portfolio into longer term investments is expected to yield a further £1.5m in 2015/16 and in particular, the strategy has changed to take account of the new risk within the market associated with 'bail in' in the event that a bank should fail.

13. Prudential Indicators

13.1. The prudential code that applies to local authorities ensures that:

- Capital programmes are affordable in revenue terms
- External borrowing and other long-term liabilities are within prudent and sustainable levels
- Treasury management decisions are taken in line with professional good practice

13.2. Some of the limits have been altered to reflect the revised treasury management and investment strategy although this does not expose the County Council to any greater levels of risk.

13.3. Appendix 8 also contains the prudential indicators required by the code for the County Council which will now be submitted for approval by the full County Council in setting the budget for 2015/16.

14. Consultation

14.1. A wide range of changes to services were approved as part of the budget setting process last year and consultation, where relevant, has taken place throughout the year through a variety of forms and methods to seek the views of interested parties. Specific statutory consultation was carried out with the business community on the budget proposals for 2015/16 and a summary of the key issues arising from this can be found at Appendix 9 to the report.

14.2. Specific changes to the budget arising from the outcome of consultation exercises have been included within Section 7 of this report.

15. Recommendations

The following decisions are sought based upon the recommendations from the Leader and Cabinet to the County Council on the 2015/16 budget and council tax, that:

15.1. The revised budget for 2014/15 contained in Appendix 1 be approved.

15.2. The one off increase in Children's Services 2015/16 cash limit of £2.8m as explained in Section 7 be approved

15.3. The updated cash limits for Departments for 2015/16 as set out in Appendix 2 are approved

15.4. The proposed service budgets for 2015/16 (which include the implications of the annual review of charges) as set out in Appendix 3 are approved.

15.5. The workforce implications of changes to the budget and the savings proposals are set out in Appendix 4 are approved.

15.6. The overall budget for the County Council for 2015/16 as set out in Appendix 5 be approved.

15.7. Estimated general balances of around £21.5 million at 31 March 2016, be approved (paragraph 10.16).

15.8. Delegated authority be given to the Director of Corporate Resources, following consultation with the Leader and the Chief Executive to make changes to the budget following Cabinet to take account of new issues, changes to figures notified by District Council's or any late changes in the final Local Government finance settlement.

15.9. **It be a recommendation to Council that**

a) The Treasurer's report under Section 25 of the Local Government Act 2003 be taken into account when the Council determines the budget and precept for 2015/16 (Appendix 7)

b) The Revised Budget set out in Appendix 1 be approved.

c) The Revenue Budget for 2015/16 (as set out in appendices 3 and 5) be approved.

d) The total **budget requirement** for the general expenses of the County Council for the year beginning 1 April 2015, be £741,358,771.

e) The **council tax requirement** for the County Council for the year beginning 1 April 2015, be £504,890,644

f) The County Council's band D council tax for the year beginning 1 April 2015 be £1,037.88 as in 2014/15

g) The County Council's council tax for the year beginning 1 April 2015 for properties in each tax band be :

	£
Band A	691.92
Band B	807.24
Band C	922.56
Band D	1,037.88
Band E	1,268.52
Band F	1,499.16
Band G	1,729.80
Band H	2075.76

h) Precepts be issued totalling £504,890,644 on the billing authorities in Hampshire, requiring the payment in such instalments and on such date set by them previously notified to the County Council, in proportion to the tax base of each billing authorities area as determined by them and as set out below:

Basingstoke and Deane	61,635.30
East Hampshire	47,352.21
Eastleigh	42,660.34
Fareham	41,630.20
Gosport	25,640.40
Hart	37,981.04
Havant	38,846.07
New Forest	69,194.00
Rushmoor	29,751.47
Test Valley	45,322.00
Winchester	46,450.38

i) The treasury management and annual investment strategies, prudential and financial health indicators for 2015/16 be approved, in accordance with the recommendations in Appendix 8.

RECOMMENDATIONS TO COUNCIL

Council is recommended to approve:

a) The Treasurer's report under Section 25 of the Local Government Act 2003 and take this into account when determining the budget and precept for 2015/16 (Appendix 7)

b) The Revised Budget set out in Appendix 1.

c) The Revenue Budget for 2015/16 (as set out in appendices 3 and 5)

d) That the total **budget requirement** for the general expenses of the County Council for the year beginning 1 April 2015, be £741,358,771.

e) That the **council tax requirement** for the County Council for the year beginning 1 April 2015, be £504,890,644.

f) That the County Council's band D council tax for the year beginning 1 April 2015 be £1,037.88 as in 2014/15

g) The County Council's council tax for the year beginning 1 April 2015 for properties in each tax band be:

	£
Band A	691.92
Band B	807.24
Band C	922.56
Band D	1,037.88
Band E	1,268.52
Band F	1,499.16
Band G	1,729.80
Band H	2,075.76

h) Precepts be issued totalling £504,890,644 on the billing authorities in Hampshire, requiring the payment in such instalments and on such date set by them previously notified to the County Council, in proportion to the tax base of each billing authorities area as determined by them and as set out below:

Basingstoke and Deane	61,635.30
East Hampshire	47,352.21
Eastleigh	42,660.34
Fareham	41,630.20
Gosport	25,640.40
Hart	37,981.04
Havant	38,846.07
New Forest	69,194.00
Rushmoor	29,751.47
Test Valley	45,322.00
Winchester	46,450.38

i) The treasury management and annual investment strategies, prudential and financial health indicators for 2015/16, in accordance with the recommendations in Appendix 8.

CORPORATE OR LEGAL INFORMATION:

Links to the Corporate Strategy

Hampshire safer and more secure for all:	yes
Maximising well-being:	yes
Enhancing our quality of place:	yes

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

Document	Location
None	

IMPACT ASSESSMENTS:

1. Equality Duty

1.1. The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited under the Act;
- Advance equality of opportunity between persons who share a relevant protected characteristic (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation) and those who do not share it;
- Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

Due regard in this context involves having due regard in particular to:

a) The need to remove or minimise disadvantages suffered by persons sharing a relevant characteristic connected to that characteristic;

b) Take steps to meet the needs of persons sharing a relevant protected characteristic different from the needs of persons who do not share it;

c) Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity which participation by such persons is disproportionally low.

1.2. **Equalities Impact Assessment:**

(a) There are no new proposals contained within this report which have not previously been considered in the 2014/15 budget report, some of which have been subject to further consideration in subsequent reports. Appropriate equalities impact screenings have been carried out in respect of these proposals. These have been used to identify where there is likely to be an impact on the service users or staff.

2. Impact on Crime and Disorder:

2.1. The County Council has a legal obligation under Section 17 of the Crime and Disorder Act 1998 to consider the impact of all the decisions it makes on the prevention of crime.

2.2. The proposals in this report are not considered to adversely affect the prevention of crime.

3. Climate Change:

3.1 How does what is being proposed impact on our carbon footprint / energy consumption?

There are no specific proposals which impact on the County Council's carbon footprint or energy consumption.

3.2 How does what is being proposed consider the need to adapt to climate change, and be resilient to its longer term impacts?

There are no specific proposals which directly relate to climate change issues.

REVENUE BUDGET – LIST OF APPENDICES

Revised Budget 2014/15

	Original Budget 2014/15	Adjustment	Adjusted Budget 2014/15	Revised Budget 2014/15	Variance
	£'000	£'000	£'000	£'000	£'000
Departmental Expenditure					
Adults	332,134	2,371	334,505	334,505	0
Children's - Schools	725,617	9,563	735,180	735,180	0
Children's - Non schools	162,365	4,464	166,829	166,829	0
Economy, Transport and Environment	113,794	1,362	115,156	115,156	0
Policy and Resources	132,806	7,976	140,782	140,782	0
TOTAL	**1,466,716**	**25,736**	**1,492,452**	**1,492,452**	**0**
Capital Financing Costs					
Committee Capital Charges	111,796	4,923	116,719	116,719	0
Capital Charge Reversal	(112,305)	(4,923)	(117,228)	(117,228)	0
Interest on Balances	(5,750)	0	(5,750)	(6,400)	(650)
Capital Financing Costs	69,862	34	69,896	66,146	(3,750)
	63,603	**34**	**63,637**	**59,237**	**(4,400)**
Pension and IAS 19 Costs					
Pensions - Int and Expected Ret on Assets	18,150	0	18,150	18,150	0
Contribution from Pension Reserve	(42,859)	(2,284)	(45,143)	(45,143)	0
IAS 19 Departments	16,722	2,284	19,006	19,006	0
Non Distributed costs	21,329	1,200	22,529	22,529	0
Soft Loan	(10)	0	(10)	(10)	0
	13,332	**1,200**	**14,532**	**14,532**	**0**
RCCO					
Main Contribution	22,050	(409)	21,641	21,641	0
Funded by Dedicated Schools Grant (DSG)	6,684	0	6,684	6,684	0
RCCO From Reserves	18,579	9,427	28,006	28,006	0
	47,313	**9,018**	**56,331**	**56,331**	**0**
Other Revenue Costs					
Contingency	21,381	(3,746)	17,635	10,411	(7,224)
Dedicated Schools Grant	(691,612)	(944)	(692,556)	(692,556)	0
Specific Grants	(120,934)	(16,054)	(136,988)	(136,988)	0
Council Tax Freeze Grant	(5,300)	(128)	(5,428)	(5,428)	0
Flood Protection Levy	606	(3)	603	603	0
Coroners Expenditure	1,331	0	1,331	1,331	0
Business Units (Net Trading Position)	(604)	199	(405)	(405)	0
	(795,132)	**(20,676)**	**(815,808)**	**(823,032)**	**(7,224)**
Net Revenue Budget	**795,832**	**15,312**	**811,144**	**799,520**	**(11,624)**

	Original Budget 2014/15	Adjustment	Adjusted Budget 2014/15	Revised Budget 2014/15	Variance
	£'000	£'000	£'000	£'000	£'000
Net Revenue Budget (Repeated)	**795,832**	**15,312**	**811,144**	**799,520**	**(11,624)**
Contributions from Earmarked Reserves					
Use of Earmarked Reserves	(22,504)	(12,971)	(35,475)	(23,851)	11,624
Trading Units Transfer to / (from) Reserves	713	(199)	514	514	0
RCCO From Reserves	(18,729)	(2,142)	(20,871)	(20,871)	0
	(40,520)	**(15,312)**	**(55,832)**	**(44,208)**	**11,624**
Balances	(7,100)	0	(7,100)	(7,100)	0
BUDGET REQUIREMENT	**748,212**	**0**	**748,212**	**748,212**	**0**

Cash Limit Calculation 2015/16

	December Cash Limit Guideline £'000	Impact of pay award £'000	Other Changes £'000	Final Cash Limit 2015/16 £'000
Adult Services	297,073	1,865	5,432	304,370
Children's - Schools	731,704	0	16,921	748,625
Children's - Non Schools	142,103	1,271	17,987	161,361
ETE	101,876	614	1,280	103,770
CCBS	33,562	1,067	(310)	34,319
Corporate Services	42,690	1,062	(223)	43,529
Public Health	40,428	0	8,778	49,206
P&R Other	7,259	25	(559)	6,725
	1,396,695	**5,904**	**49,306**	**1,451,905**

Notes :

The increase to the Adult Services cash limit mainly reflects the addition of new burdens funding for increased costs associated with the implementation of the Care Bill.

The increase for Schools in partly due to an increase in Dedicated Schools Grant due to increased pupil numbers and the expected carry forward of 14-15 grant. There is also an expected increase in funding for Universal Free Schools Meals.

The increase for Children’s Services (non schools) is mainly due to the addition of £12.5m to support pressures in the Children Looked After budget and the one off addition of £2.8m following the outcome of public consultations on budget proposals.

The increase for ETE is mainly due to the addition of the Bus Service Operators Grant.

The increase for Public Health is due to the inclusion of part year funding for Children aged 0 to 5.

Within Policy & Resources other, a decrease due to the loss of the Local Welfare Provision Grant has been partially offset by increased grant funding for the Supporting Troubled Families Programme.

Adult Services
Budget Summary 2015/16

Service Activity	Original Budget 2014/15 £000	Revised Budget 2014/15 £000	Proposed Budget 2015/16 £000
Service Strategy and Regulation	515	545	507
Older People (aged 65 or over)	134,572	137,976	121,711
Adults under 65 years with Physical or Sensory Impairment	34,095	34,650	34,937
Adults under 65 years with Learning Disabilities	112,108	113,566	108,240
Adults under 65 years with Mental Health Needs	13,109	13,327	13,102
Supported Employment	484	489	489
Other Adult Services	3,057	1,664	1,387
Supporting People	21,433	24,020	13,798
Unallocated Budget	12,426	7,933	9,864
Non-distributed Costs	335	335	335
Total	**332,134**	**334,505**	**304,370**

Children's Services
Budget Summary 2015/16

Service Activity	Original Budget 2014/15 £000	Revised Budget 2014/15 £000	Proposed Budget 2015/16 £000
Schools budget			
Individual Schools budgets	526,944	525,594	530,830
De-delegated items	3,953	3,909	3,950
High Needs block	84,861	83,786	85,901
Early Years block	59,959	61,927	61,668
Central Provision within schools budget	9,211	10,656	10,012
Other grants	40,689	49,308	56,264
Total Schools Budget	**725,617**	**735,180**	**748,625**
Non-schools budget			
Other Education & Community – Special Education	4,924	7,354	5,267
Other Education & Community – Learner Support	33,420	33,302	33,099
Other Education & Community – Access	693	467	413
Young People's Learning Development	1,056	1,014	1,035
Adult Learning and Community	149	269	269
Services for Young Children	17,032	16,144	8,763
Youth Support Services	6,710	6,755	5,366
Strategic Management	4,761	5,103	4,151
Assessment and Care Management	19,501	19,691	19,714
Children Looked After	46,044	46,107	58,211
Family Support Services	15,328	15,469	14,369
Youth Justice	2,175	2,574	2,219
Other Children and Families Services	7,714	8,940	7,695
Asylum Seekers	493	493	500
Central Budgets	2,365	3,147	20
Total Non-schools budget	**162,365**	**166,829**	**161,361**
Total Children's Services budget	**887,982**	**902,009**	**909,986**

ETE
Budget Summary 2015/16

Service Activity	Original Budget 2014/15 £000	Revised Budget 2014/15 £000	Proposed Budget 2015/16 £000
Highways Maintenance	32,144	32,131	31,437
Public Transport	19,481	19,863	18,884
School Crossing Patrols	1,132	1,145	1,155
Road Safety	789	780	526
Traffic Surveys	87	87	86
Parking Services	-97	-97	-99
Staffing & Operational Support (Highways & cross-departmental)	13,536	13,559	13,449
Total Highways, Traffic and Transport	**67,072**	**67,468**	**65,438**
Waste Disposal Contract	38,389	37,192	34,627
Waste Management non-contract	1,185	908	930
Planning and Development	1,913	1,939	1,640
Chichester Harbour Conservancy	187	187	187
Total Waste, Planning and Environment	**41,674**	**40,226**	**37,384**
Economic Development	986	1,105	948
Early achievement of savings – firm proposals	4,062	6,357	0
Total – Cash Limit	**113,794**	**115,156**	**103,770**

Policy & Resources
Budget Summary 2015/16

Service Activity	Original Budget 2014/15 £000	Revised Budget 2014/15 £000	Proposed Budget 2015/16 £000
Culture, Communities and Business Services:			
Business Services	181.0	299.0	155.0
Rural Broadband	93.0	113.0	94.0
Sir Harold Hillier Gardens	472.0	439.0	412.0
Office Accommodation/Workstyle	7,212.0	6,687.0	5,642.0
Facilities Management	2,870.0	3,083.0	2,925.0
Community:			
Regulatory Services	3,825.0	2,598.0	1,807.0
Community Grants & Policy Fund	1,680.0	1,511.0	1,472.0
Sport	210.0	264.0	196.0
Community	343.0	270.0	303.0
Library Service	12,970.0	12,925.0	12,410.0
Business Support	1,212.0	1,758.0	799.0
Culture & Heritage:			
Countryside	3,053.0	3,152.0	2,881.0
Outdoors Centres	443.0	637.0	385.0
Arts & Museums	2,895.0	3,264.0	2,989.0
Archives	956.0	969.0	892.0
Risk, Health & Safety	209.0	211.0	214.0
Property Services:			
Direct Services	-893.0	-848.0	-966.0
Repair and Maintenance	-541.0	-447.0	-905.0
Property Services	1,271.0	1,502.0	1,337.0
CCBS Planned contribution to Cost of Change	0.0	2,619.0	1,277.0

	Original Budget 2014/15 £000	Revised Budget 2014/15 £000	Proposed Budget 2015/16 £000
Other Direct Services:			
Public Health:			
- Central Public Health	2,349.0	2,416.0	2,482.0
- Information and Intelligence	39.0	39.0	39.0
- Nutrition, Obesity and Physical Activity	1,810.0	2,636.0	1,594.0
- Drugs & Alcohol	9,439.0	9,479.0	9,475.0
- Tobacco	3,149.0	3,149.0	3,149.0
- Dental	180.0	180.0	180.0
- Children 5-19	6,161.0	4,121.0	4,121.0
- Children under 5	0.0	0.0	8,843.0
- Health Checks	1,447.0	1,447.0	1,527.0
- Miscellaneous Health Imp & Wellbeing	4,204.0	5,851.0	6,351.0
- Sexual Health	11,534.0	11,534.0	11,329.0
- Infection, Prevention & Control	116.0	116.0	116.0
- Transitional costs	0.0	37.0	0.0
Grants to Voluntary Organisations	271.0	247.0	247.0
Grants/Contributions to Councils of Community Service and Other Bodies	1,013.0	1,013.0	888.0
Members Devolved Budgets	624.0	624.0	624.0
Supporting Troubled Families	939.0	4,656.0	1,622.0
Other Direct and Corporate Services	822.0	919.0	664.0
Corporate Services:			
Policy & Governance:			
- Legal	2,028.0	2,353.0	2,272.0
- Governance	1,389.0	1,478.0	1,453.0
- Performance & Communications	1,576.0	1,696.0	1,510.0
- Transformation	1,591.0	2,079.0	1,867.0
Strategic Business Development	1,226.0	0.0	0.0
Corporate Resources:	0.0	0.0	0.0
- CBS	8,601.0	8,257.0	7,165.0
- HR	1,916.0	2,688.0	2,623.0
- Finance	5,164.0	5,293.0	4,194.0
- IT	19,144.0	19,732.0	18,465.0
Other Corporate Services	4,945.0	5,033.0	3,980.0

	Original Budget 2014/15 £000	Revised Budget 2014/15 £000	Proposed Budget 2015/16 £000
Members Support Costs	1,748.0	1,703.0	1,706.0
Other Central Support Services	920.0	1,000.0	974.0
Total P&R Cash Limited Services	**132,806.0**	**140,782.0**	**133,779.0**
Coroners	1,331.0	1,331.0	1,331.0
Transfers (to) / from reserves:			
School Library Service	-48.0	54.0	-48.0
Hampshire Wardrobe	0.0	0.0	0.0
River Hamble	-27.0	-27.0	-27.0
Caretaking and Cleaning Support Service	0.0	0.0	0.0
Segensworth Unit Factories	-12.0	-12.0	-12.0
Hampshire Printing Services	-33.0	-33.0	-30.0
Corporate Procurement County Supplies	-92.0	-110.0	-141.0
HC3S	-398.0	-398.0	-484.0
Hampshire Transport Management (HTM)	-51.0	-51.0	0.0
EFS	0.0	0.0	0.0
EPS	-113.0	-113.0	-113.0
Government Grants:			
Inshore Fisheries and Conservation	-204.0	-204.0	-204.0
Supporting Troubled Families	-639.0	-1,409.0	-1,622.0
Local welfare reform		-1,573.0	
Local Reform and Community Voices	-540.0	-540.0	-540.0
Public Health	-40,428.0	-41,005.0	-49,206.0
Total net expenditure	**91,552.0**	**96,692.0**	**82,683.0**

Workforce Statement (Full Time Equivalent)

Department / Service	Base Position FTE's	Estimated FTE's at 31/03/2016	Net Variation
Adult Services	2,828	2,795	(33)
Children's Services - Non schools	2,494	2,441	(53)
Economy, Transport and Environment	704	704	0
Policy and Resources	3,755	4,060	305
	9,781	10,000	219

Staffing variations are:	Transfers and other changes	Impact of new savings proposals	Total 2015/16 changes
Adult Services			
Impact of savings proposals		(33)	(33)
Children's Services - Non schools			
Impact of savings proposals		(77)	(77)
Other net changes	24		24
Policy and Resources			
Increase due to TUPE of staff into H3	203		203
Increase in HC3S due to increased take up of free schools meals	102		102
Other net changes	31		31
Impact of saving proposals		(31)	(31)
	360	(141)	219

Revenue Budget 2015/16

	Original Budget 2014/15	Adjustment	Budget 2015/16
	£'000	£'000	£'000
Departmental Expenditure			
Adults	332,134	(27,764)	304,370
Children's - Schools	725,617	23,008	748,625
Children's - Non schools	162,365	(1,004)	161,361
Economy, Transport and Environment	113,794	(10,024)	103,770
Policy and Resources	132,806	973	133,779
	1,466,716	**(14,811)**	**1,451,905**
Capital Financing Costs			
Committee Capital Charges	111,796	4,923	116,719
Capital Charge Reversal	(112,305)	(4,923)	(117,228)
Interest on Balances	(5,750)	(1,500)	(7,250)
Capital Financing Costs	69,862	(966)	68,896
	63,603	**(2,466)**	**61,137**
Pension and IAS 19 Costs			
Pensions - Int and Expected Ret on Assets	18,150	0	18,150
Contribution from Pension Reserve	(42,859)	(2,984)	(45,843)
IAS 19 Departments	16,722	2,984	19,706
Non Distributed costs	21,329	2,100	23,429
Soft Loan	(10)	0	(10)
	13,332	**2,100**	**15,432**
RCCO			
Main Contribution	22,050	509	22,559
Funded by Dedicated Schools Grant (DSG)	6,684	(428)	6,256
RCCO From Reserves	18,579	(12,991)	5,588
	47,313	**(12,910)**	**34,403**
Other Revenue Costs			
Contingency	21,381	11,828	33,209
Dedicated Schools Grant	(691,612)	(7,005)	(698,617)
Specific Grants	(120,934)	(30,458)	(151,392)
Council Tax Freeze Grant	(5,300)	(175)	(5,475)
Flood Protection Levy	606	(3)	603
Coroners Expenditure	1,331	0	1,331
Business Units (Net Trading Position)	(604)	34	(570)
	(795,132)	**(25,779)**	**(820,911)**
Net Revenue Budget	**795,832**	**(53,866)**	**741,966**

	Original Budget 2014/15	Adjustment	Budget 2015/16
	£'000	**£'000**	**£'000**
Net Revenue Budget (Repeated)	**795,832**	**(53,866)**	**741,966**
<u>Contributions from Earmarked Reserves</u>			
Use of Earmarked Reserves	(22,504)	27,556	5,052
Trading Units Transfer to / (from) Reserves	713	(34)	679
Business Strategy Opportunities	0	(1,500)	(1,500)
RCCO From Reserves	(18,729)	12,991	(5,738)
	(40,520)	**39,013**	**(1,507)**
Use of General Balances	(7,100)	8,000	900
BUDGET REQUIREMENT	**748,212**	**(6,853)**	**741,359**

Reserves Strategy

Introduction

The level and use of local authority reserves has been a regular media topic over a number of years often fuelled by comments from Government that these reserves should be used to significantly lessen the impact of the austerity measures, that have seen a greater impact on local government than any other sector.

The County Council has continually explained that reserves are kept for many different purposes and that simply trying to bridge the requirement for long term recurring savings through the use of reserves only seeks to use up those reserves very quickly (and mean that they are not available for any other purposes) and merely delays the point at which the recurring savings are required.

At the end of the 2013/14 financial year the County Council's earmarked reserves together with the general fund balance stood at nearly £482m an increase of £63m on the previous year. This Appendix sets out in more detail what those reserves are for and outlines the strategy that the County Council has adopted and articulated in using reserves and more importantly in contributing to them.

Reserves Position 31 March 2014

Current earmarked reserves together with the General Fund balance totalled £481.7m at the end of the 2013/14 financial year. The table below summarises by purpose the total level of reserves and balances that the County Council holds and compares this to the position reported at the end of 2012/13.

The narrative beneath the table explains in more detail the purpose for which the reserves are held and in particular why the majority of these reserves cannot be used for other reasons.

	Balance 31.3.2013 £'000	Balance 31.3.2014 £'000	% of Total %
Fully Committed to Existing Spend Programmes			
Capital Grants Unapplied	74,967	71,778	14.9%
Revenue Grants Unapplied	18,448	40,667	8.4%
General Capital Reserve	89,316	129,272	26.8%
Street Lighting Reserve	2,395	3,893	0.8%
Community Transport Reserve / Other	1,550	1,651	0.3%
	186,676	**247,261**	**51.2%**
Departmental / Trading Reserves			
Trading Accounts	13,780	14,691	3.0%
Departmental - Cost of Change Reserve	30,601	30,543	6.3%
	44,381	**45,234**	**9.3%**

	Balance 31.3.2013 £'000	Balance 31.3.2014 £'000	% of Total %
Risk Reserves			
Insurance Reserve	22,043	24,837	5.2%
Local Government Resource Review	6,150	6,150	1.3%
	28,193	**30,987**	**6.5%**
'Available' Reserves			
Corporate Policy Reserve	1,979	3,676	0.8%
Invest to Save	10,154	10,073	2.1%
Corporate Efficiency Reserve	9,235	8,931	1.9%
Organisational Change Reserve	10,018	7,854	1.6%
Grant Equalisation Reserve	48,460	50,464	10.5%
	79,846	**80,998**	**16.9%**
HCC Earmarked Reserves	**339,096**	**404,480**	**84.0%**
Schools Reserves	44,870	49,572	10.3%
Total Earmarked Reserves	**383,966**	**454,052**	**94.3%**
General Fund Balance	34,795	27,697	8.3%
Total Reserves and Balances	**418,761**	**481,749**	**100.0%**

Fully Committed to Existing Spend Programmes

These reserves, which account for over half of total reserves are already fully committed in the main to existing revenue or capital programmes. They really represent the extent to which resources, in the form of government grants or revenue contributions to capital, are received or generated in advance of the actual spend on the project.

Specifically, the street lighting reserve represents the anticipated surplus generated by the financial model for this PFI scheme that is invested up front and then applied to the contract payments in future years.

These reserves have increased significantly in recent years following a change to International Financial Reporting Standards which required unapplied government grants to be shown as earmarked reserves and due to the fact that significant revenue contributions have been made to fund future capital investment using the surplus funds generated from the early achievement in savings (a deliberate strategy that is explained in more detail later in this paper).

These reserves do not therefore represent 'spare' resources in any way and account for the majority of the increase between 2012/13 and 2013/14.

Departmental / Trading Reserves

Trading services within the County Council operate as semi-commercial organisations and as such they do not receive specific support from the County Council in respect of capital investment or annual pressures arising from spending or income fluctuations.

Given this position, any surpluses generated by the trading services are earmarked for their use to apply for example to equipment renewal, service expansion, service improvement, innovation and marketing. They are also used to smooth cash flows between years if deficits are made due to the loss of the customer base and provide the time and flexibility to generate new revenues to balance the bottom line in future years.

Departmental reserves are generated through under spends in annual revenue expenditure and Council policy was changed in 2010 to allow Departments to retain all of their under spends in order to provide resources to :-

- Meet any potential overspends in future years without the need to call on corporate resources
- Manage cash flow funding issues between years where specific projects may have been started but not fully completed within one financial year.
- Meet the cost of standard redundancy and pension payments arising from the down sizing of the work force
- Invest in new technology and other service improvements, for example the new Children's Services integrated system
- Undertake capital repairs or improvements to assets that are not funded through the existing capital programme where this is essential to maintain service provision or maximise income generation.
- Meet the cost of significant change programmes and restructures such as the Corporate Services Review implementation, which is being fully funded from planned savings within the Corporate Services Department.

By utilising reserves in this way, and allowing Departments and Trading areas to retain under spends or surpluses it encourages prudent financial management as managers are able to ensure that money can be re-invested in service provision without the need to look to the corporate centre to provide funding. This fosters strong financial management across the County Council and is evidenced by the strong financial position that the County Council is in at this point in time.

Risk Reserves

The Council holds specific reserves to mitigate risks that it faces. The County Council self insures against certain types of risks and the level of the insurance reserve is based on an independent valuation of past claims experience and the level and nature of current outstanding claims.

On 1st April 2013, the Government introduced two new schemes that have an impact on the financial stability of local government. Business rates retention transferred both risk and potential reward to local authorities in that a proportion of locally generated business rates is now retained by local councils and fire authorities. Whilst this does introduce the potential for this income base to grow if there is economic growth, it also means that there is the potential for lost income should the business rate base decline.

In addition, local Council Tax Support Schemes were introduced on 1st April and replaced the national scheme for council tax benefits. The national funds were distributed amongst authorities to compensate for the loss of council tax income, but these were reduced by 10%. On top of this reduction in funding, Councils face further risk in the form of increasing numbers of claimants due to economic factors or due to the increased publicity around the schemes. If claimant numbers increase, the Government does not provide any additional funding and therefore the costs of this fall on the local authorities.

Both of these changes represent a significant risk transfer from central to local government and therefore a separate risk reserve has been created to mitigate potential losses arising from these sources in order to soften the impact on the budget setting process in any one year. Given that we are now into the second full year of implementation, a review of the need for these and other reserves will be undertaken as part of the final accounts process for 2014/15.

'Available' Reserves

The above paragraphs have explained that the majority of reserves are set aside for specific purposes and are not available in general terms to support the revenue budget or for other purposes.

This leaves other available earmarked reserves that are under the control of the County Council and total nearly £81m at the end of last financial year. Whilst it is true to say that these reserves could be used to mitigate the loss of Government grant reductions, the County Council has decided to take a more sophisticated long term approach to the use of these reserves, that brings many different benefits both directly and indirectly to the County Council and residents of Hampshire. They are broken down into four main areas :-

Corporate Policy Reserve – This small reserve is available to fund new budget initiatives that are agreed as part of the overall budget. It offers the opportunity to introduce specific service initiatives that might not have otherwise gained funding and are designed to have a high impact on service users or locations where they are applied. Past initiatives have included :

- Targeted speech and language therapy
- Apprenticeship and graduate placement schemes
- Funding for rural grants
- Funding for troubled families programme
- Olympic legacy
- The 'Have Your Say' community bidding budget

Invest to Save / Corporate Efficiency Reserve – These reserves are earmarked to provide funding to help transform services in order to make further revenue savings in the future. Rather than just prop up the budget on a short term basis, the County Council feels it is a far more sensible policy to use available reserves to generate savings and improve services over the longer term, by re-designing services and investing in technology and other solutions that make services more modern and efficient.

Organisational Change Reserve – The County Council is one of the largest employers in Hampshire and inevitably, large reductions in Government grant leading to reduced budgets means that there is a significant impact on the numbers of staff that are employed in the future.

The County Council as a good employer has attempted to manage the reduction in staff numbers as sensitively and openly as possible and introduced an enhanced voluntary redundancy scheme back in 2011. The scheme offers an enhanced redundancy rate for people who elect to take voluntary redundancy and this has been a highly successful way of managing the reductions in staff numbers, whilst maintaining morale within the rest of the workforce who are not required to go through the stress and uncertainty of facing compulsory redundancies.

In fact, since the scheme was introduced, voluntary redundancies account for around 98% of the total number of staff that have left the organisation as a result of specific restructures and service re-design.

As explained above, Departments are still responsible for meeting the ‘standard’ element of any redundancy package, but the Organisational Change Reserve was put in place to meet the ‘enhanced’ element of the payment. The reserve was recently topped back up to provide funding to continue the voluntary redundancy scheme as part of the TtC to 2015 programme and will need to be further reviewed in the context of the current (and final) Enhanced Voluntary Redundancy process currently being carried out.

Grant Equalisation Reserve – This reserve was set up many years ago to deal with changes in Government grant that often came about due to changes in distribution methodology that had an adverse impact on Hampshire compared to other parts of the country.

In 2010/11, the County Council recognised that significant reductions in local government spending were expected and built in contributions as part of the Medium Term Financial Strategy over the CSR 2010 period from the Grant Equalisation Reserve in order to smooth the impact of the grant reductions.

Over the last few years, it has become clear that the period of austerity will continue for much longer than planned and therefore the County Council has taken the opportunity to increase the reserve in order to be able to continue the sensible policy of smoothing the impact of grant reductions without the need to make ‘knee jerk’ reactions to offset large decreases in grant

It should be highlighted that the total ‘Available Reserves’ outlined above account for only 16.9% of total reserves and balances that the County Council holds and of these, the majority have been set aside as part of a longer term strategy for dealing with the significant financial challenges that have been imposed on the County Council.

The reserves detailed above represent the total earmarked reserves of the County Council and amount to £404.5m as shown in the table on page 2 of this Appendix. In addition, the County Council is required to show schools reserves as part of its accounts and it must hold a minimum level of general balances, both of which are outlined below.

Schools Reserves

Schools reserves account for nearly £49.6M or 10.3% of total reserves and balances. These reserves must be reported as part of the County Council's accounts, but since funds are delegated to schools any surplus is retained by them for future use by the individual school concerned. Similarly, schools are responsible for any deficits in their budgets and they maintain reserves in a similar way to the County Council in order to smooth fluctuations in cash flow over several years.

The County Council has no control at all over the level or use of school reserves.

General Fund Balance

The General Fund Balance is the only reserve that is in effect not earmarked for a specific purpose. It is set at a level recommended by the Chief Financial Officer at around 2.5% of the budget requirement and in effect it represents a working balance of resources that could be used at very short notice in the event of a major financial issue.

The current balance stands at £27.7m, which includes £8m carried forward from the 2012/13 financial year that will be used to provide planned contingency support of £8m in the current financial year. After this planned usage, the balance will return back to the recommended minimum of around 2.5% of the budget requirement (£19.7m).

Reserves Strategy

The County Council's approach to reserves has been applauded in the past by the Government and the External Auditors as a sensible, prudent approach as part of a wider Medium Term Financial Strategy. This has enabled the County Council to make savings and changes in service delivery in a planned and controlled way rather than having to make urgent unplanned decisions in order to reduce expenditure.

This approach is well recognised across local government and an article in the Municipal Journal by the Director of Local Government at the Chartered Institute of Public Finance and Accountancy stated :

"What reserves do allow authorities to do is to take a more medium term view of savings and expenditure and make decisions that give the best value for money. This is better than having to make unnecessary cost reductions in the short term because they do not have the money or funding cushion to allow for real transformation in the way they provide services."

It is now clear that the period of austerity will last longer than anyone had previously predicted and therefore it is possible that the County Council will have to take a longer term view of its financial strategy than the traditional 3 to 4 years that it has used in the past. A core strand of this strategy going forward will be the continued use and replenishment of reserves in line with the strategy and ensuring that there is sufficient financial capacity to cope with the challenges ahead, possibly up to 2020.

The County Council's strategy for reserves is already well established and is based on a cyclical pattern as follows :

- Planning ahead of time and implementing efficiencies and savings in advance of need
- Generating surplus funds in the early part of the programme
- Using these resources to fund investment and transformation in order to achieve the next phase of savings.

This cycle was clearly evident during the last 3 financial years, with surplus funds generated in advance of need as part of budget setting and then supplemented by further savings in the year. Savings in advance of need within Departments and savings in contingency amounts due to the successful implementation of the full early savings programme meant that the Council was able to provide :

- Departmental reserves to pay for the cost of change associated with their own transformation programmes
- Top up funding to the organisational change reserve to provide resources to continue the very successful voluntary redundancy programme as a means of releasing staff in a sensitive and controlled manner that has helped maintain morale across the Council
- An additional £5m within the Invest to Save Reserve to help with the Transforming the Council to 2015 programme that will deliver the next phase of savings to 2015/16.
- Additional funds for the Grant Equalisation Reserve to help smooth the impact of grant reductions and give the County Council maximum flexibility in future budget setting processes

The Transforming the Council to 2015 programme has already generated early savings in 2014/15 that will increase the level of balances this year, albeit there will be planned reductions and use of reserves in line with the strategy outlined in this Appendix.

Looking further ahead, a similar strategy will be applied in looking to make savings up to 2017/18, allowing planned reductions to be made and providing resources to support the next transformation programme.

It is important to highlight that the strategy the County Council has adopted means that if we are in a position that reserves begin to decrease, it may be a sign that there is something wrong within the savings programme or financial strategy that might therefore need to be addressed. In any event, it needs to be stressed that the strong financial position that the County Council finds itself in is not an accident and is one about which we should be proud.

Section 25 report, Local Government Act 2003

Section 25 of the Act requires the Chief Financial Officer (the Director of Corporate Resources) to report to the County Council when setting its council tax on:

- the robustness of the estimates included in the budget
- the adequacy of the financial reserves in the budget.

The County Council is required to have regard to this report in approving the budget and council tax. It is appropriate for this report to go first to Cabinet and then made available to the County Council in making its final decision.

The CIPFA guidance on reserves and balances provides the general framework for considering the adequacy of reserves. A risk assessment has been made of the cost and demand pressures on budgets, insurance liabilities, achievement of budget savings and adverse winter conditions which support the proposed level of general balances of approximately £21.5m forecast for the end of 2015/16. This assessment has not changed significantly from last year and must also be set in the context of new contingency amounts proposed in the budget that mitigate the key risks that have been identified.

Similarly the level of reserves is scrutinised each year and a reserves strategy for the purpose, use, control and review of reserves has previously been agreed and remains in place. Details of the key earmarked reserves is contained in Appendix 6/7 of the revenue report, but in addition, Schools have one of the largest reserves at a projected £49m supporting their delegated budgets funded by ring-fenced specific grant. The most important reserves for other services in terms of the medium term view are the grant equalisation reserve (used to help match grant loss), corporate efficiency reserve and the insurance reserve.

Section 25 concentrates primarily on the uncertainty within the budget year rather than the greater uncertainties in future years. However future uncertainties, particularly for the County Council in respect of the impact of continued period of austerity have been taken into account in devising the Medium Term Financial Strategy and the levels of reserves required to support it.

The budget report is the conclusion of a detailed process of prior consultation and consideration throughout the current year by Cabinet.

The County Council’s policy on balances is to hold a minimum prudent level which on the basis of the previous risk assessment is 2.6% of net expenditure. The projected level of general fund balances will be 2.9% of net expenditure at the end of 2015/16, which reflects the declining level of spend rather than an increase in the level of balances held. However, the risks associated with being a floor authority and thus receiving the biggest reduction in government grant and of needing to achieve significant savings in service expenditure to balance the budget continue to justify this level of reserves.

The level of uncertainty for the budget year is also narrowed down as the budget strategy is developed during the year and defined in the performance and risk management and earmarked reserves paragraphs in the budget report.

In setting the budget the County Council should have regard to the strategic, operational and financial risks facing the County Council. The County Council has an overall risk management framework which covers these issues. The forward budget plan and reserves take into account the main risks and uncertainties, including:

- Inflation

  - Average pay inflation of 2.4% was awarded across the two year of 2014/15 and 2015/16 and is already reflected in the budget.

  - price inflation has been set at 2.2%. Given the volatility of both the retail and consumer price indices during the last year, containing price increases at an average 2.2% may prove challenging, depending upon market factors.

  - short-term interest rates remain low and base rates are not expected to increase for some time. However, this does mean that any long term borrowing carried out in 2015/16 attracts a high ‘cost of carry’ since longer term rates are influenced by gilt prices and not the current base rate. Decisions on when long term borrowing is undertaken will therefore have an impact on the revenue account next year.

- Pay drift

  - increments are not budgeted for and services will need to secure efficiency savings to offset these. Past trends suggest that this can be managed.

- Employer contributions for the current service contribution will remain at the same level until the next tri-ennial valuation and the budget already includes allowance for the increased costs of recovering the past deficit contribution in lne with the agreed strategy over the next 5 years.

- Savings and redeployments built in to the budget

  - The Transformation to 2015 Programme is currently being implemented in order to achieve savings of £102.5m in the next financial year. continued string robust management of the County council’s finances will be critical over the next year particularly as focus will also turn to the development and approval of the next Transformation Programme to 2017.

- Income

  - there is an annual review to maximise and increase income at least in line with costs which is referred to in Section 7 of the report and reported in greater detail to Executive Members. The increased reliance on the generation of income as a means of closing the budget gap exposes the County Council to greater levels of risk compared to reducing budgets outright. The total level of 'sold services' and other income contributions across the County Council is now in the region of £100m and a specific risk contingency has therefore been included to mitigate this risk in the revenue budget.

- Achievement of budget plan

  - There is a well established and sound history of very close achievement of outturn to budgets, which is further supported by performance during 2014/15 which is predicting spend within budget across all Departments after take account of central support already agreed and the use of Departmental contingencies and cost of change reserves.

- Strength of financial information and reporting arrangements

  - Budget monitoring throughout the year is now based on a much greater risk based approach across the Departments in the County Council, although monitoring for 2014/15 has been affected by changes arising from the new systems that have been introduced. This was expected and it is anticipated that monitoring information for 2015/16 will be more robust.

- Capital programme

  - capital strategy, asset management plans and the local transport plan have all previously been accredited with the highest scores in the former comprehensive performance assessment.

  - Despite reductions in capital receipts over the last few years, the capital programme has been supplemented by additional revenue contributions that have allowed high priority investment to proceed.

  - A capital review undertaken in the summer of last year ensured that the existing programme is focussed on the correct priorities for the county council and adjustments were made to take account of new issues, in particular, the need to provide for flood mitigation measures following the severe floods across Hampshire last year.

- Level of borrowing and outstanding debt

  - the issues are fully covered in the treasury management strategy and prudential indicators appendix to the budget report.

  - the current policy on temporary unsupported borrowing for specific projects results in the financing costs being contained within the forward budget plan cash limits without an additional impact on the council tax payer.

  - despite much lower capital receipts than originally planned since 2008/09, it has been possible to avoid the need for temporary unsupported borrowing to cover a general shortfall in capital financing resources.

- Contingent Liabilities

  - the County Council self-insures, so it finances all its own liability claims. The liabilities are uncertain but to cover these a provision is maintained for known liability claims and a reserve is maintained to deal with fluctuations in liabilities and in the level of fire damage reinstatement, which now stands at nearly £25m.

- Annual Governance Statement

  - the Director of Corporate Resources has the responsibility for ensuring that an effective system of internal financial control is maintained and operated in connection with the resources concerned.

  - the review of the effectiveness of the system of internal financial control is informed by the work of the managers within the County Council, by internal audit and the external auditors in its annual governance report and other reports.

  - the Audit Committee receives and reviews the annual governance statement and the external audit governance report.

- External Audit

  - gave an unqualified opinion on the 2013/14 accounts, and an unqualified opinion on the County Council's arrangements to secure economy, efficiency and effectiveness in its use of resources in 2013/14.

- Other risks

    - there are potential legal claims outstanding and other possible risks which past trends suggest can be met from balances if required. There is no known significant risk or liability which requires a provision, contingency or reserve not already allowed for in the budget report.

    - changes in function and funding arrangements. The main risk relates to the arrangements for transferring funding from the County Council in respect of central services to schools, as schools opt for Academy status. The loss has been allowed for in the 2015/16 budget without assuming any offsetting savings will necessarily arise in the year.

Provided that the County Council considers the above factors and accepts the budget recommendations, including the level of earmarked reserves and balances, a positive opinion can be given under Section 25 on the robustness of the estimates and level of reserves.

Carolyn Williamson

Director of Corporate Resources

23rd January 2015

Treasury Management Strategy and Investment Strategy 2015/16 to 2017/18

1. Summary

1.1. The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the CIPFA Code) and the Prudential Code require authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators (PIs) on an annual basis. The TMSS also includes the Annual Investment Strategy (AIS) that is a requirement of the Department for Communities and Local Government's (DCLG) Investment Guidance.

1.2. As per the requirements of the Prudential Code, Hampshire County Council adopted the CIPFA Treasury Management Code at its meeting in February 2012. This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the CLG Guidance.

1.3. The purpose of this TMSS is, therefore, to approve:

- Treasury Management Strategy for 2015/16
- Annual Investment Strategy for 2015/16, including proposals for changes to the investment of the County Council's cash balances to increase the yield earned on investments
- Prudential Indicators for 2015/16, 2016/17 and 2017/18 shown in Appendix C
- Minimum Revenue Provision (MRP) Statement shown in Appendix D

1.4. The County Council has potentially large exposures to financial risks through its investment and borrowing activity, including the loss of invested funds and the effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's treasury management strategy.

1.5. **This Report recommends the following be approved:**

- **Treasury Management Strategy and Annual Investment Strategy for 2015/16 (and the rest of 2014/15) including:**
    - **Prudential Indicators for 2015/16, 2016/17 and 2017/18 – Appendix C**
    - **Minimum Revenue Provision (MRP) Statement – Appendix D**
    - **That authority is delegated to the Director of Corporate resources to manage the Council's investments according to the risk assessment process in the Investment Strategy as appropriate to most effectively manage the Council's investments.**

- **An additional reserve of £0.5m is created in the County Council's accounts as protection against the irrecoverable fall in value of any investments.**

2. Introduction

2.1. In February 2012 the County Council adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code) which requires the County Council to approve a treasury management strategy before the start of each financial year.

2.2. In addition, the Department for Communities and Local Government (DCLG) issued revised Guidance on Local Authority Investments in March 2010 that requires the County Council to approve an investment strategy before the start of each financial year.

2.3. This report fulfils the County Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the DCLG Guidance.

2.4. The County Council has potentially large exposures to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the County Council's treasury management strategy.

3. External Context

3.1. The following paragraphs explain the economic and financial background against which the Treasury Management Strategy is being set.

Economic background

3.2. There is momentum in the UK economy, with a continued period of growth through domestically-driven activity and strong household consumption. There are signs that growth is becoming more balanced. The greater contribution from business investment should support continued, albeit slower, expansion of GDP. However, inflationary pressure is currently extremely benign and is likely to remain low in the short-term. There have been large falls in unemployment but levels of part-time working, self-employment and underemployment are significant and nominal earnings growth remains weak and below inflation.

3.3. The Bank of England's Monetary Policy Committee's (MPC) focus is on both the degree of spare capacity in the economy and the rate at which this will be used up, factors prompting some debate on the Committee. Despite two MPC members having voted for a 0.25% increase in rates at each of the meetings between August and December 2014, the minutes of the January 2015 meeting showed unanimity in maintaining the Bank Rate at 0.5% as there was sufficient risk that low inflation could become entrenched and the MPC became more concerned about the economic outlook.

Interest rate forecast

3.4. The County Council's treasury management advisor Arlingclose forecasts the first rise in official interest rates in August 2015 and a gradual pace of increases thereafter, with the average for 2015/16 being around 0.75%. Arlingclose believes the normalised level of the Bank Rate post-crisis to range between 2.5% and 3.5%. The risk to the upside (i.e. interest rates being higher) is weighted more towards the end of the forecast horizon. On the downside, Eurozone weakness and the threat of deflation have increased the risks to the durability of UK growth. If the negative indicators from the Eurozone become more entrenched, the Bank of England will likely defer rate rises to later in the year. A more detailed economic and interest rate forecast provided by the Arlingclose is attached at Appendix A.

Credit outlook

3.5. The transposition of two European Union directives into UK legislation in the coming months will place the burden of rescuing failing EU banks disproportionately onto unsecured local authority investors. The Bank Recovery and Resolution Directive promotes the interests of individual and small businesses covered by the Financial Services Compensation Scheme and similar European schemes, while the recast Deposit Guarantee Schemes Directive includes large companies into these schemes. The combined effect of these two changes is to leave public authorities and financial organisations (including pension funds) as the only senior creditors likely to incur losses in a failing bank after July 2015.

3.6. The continued global economic recovery has led to a general improvement in credit conditions since last year. This is evidenced by a fall in the credit default swap spreads of banks and companies around the world. However, due to the above legislative changes, the credit risk associated with making unsecured bank deposits will increase relative to the risk of other investment options available to the County Council. Whilst the likelihood of suffering a loss from the default of a bank remains relatively unchanged, the 'bail-in' regime has significantly increased the impact a default would have in terms of the scale of loss the County Council could be exposed to.

4. Local Context

4.1. As at 31 December 2014 the County Council had £541m of borrowing and £540m of investments. This is set out in further detail at Appendix B. Forecast changes in these sums are shown in the balance sheet analysis in Table 1.

Table 1: Balance Sheet Summary and Forecast

	31.03.14 Actual £m	31.03.15 Estimate £m	31.03.16 Estimate £m	31.03.17 Estimate £m	31.03.18 Estimate £m
Capital Financing Requirement	759	771	765	741	702
Less: Other long-term liabilities					
- Street lighting PFI	(90)	(120)	(116)	(113)	(109)
- Waste management contract	(70)	(65)	(60)	(55)	(49)
Borrowing CFR	599	586	589	573	544
Less: External borrowing					
- Public Works Loan Board	(296)	(281)	(270)	(257)	(243)
- Market Loans (LOBOs)	(73)	(73)	(73)	(73)	(73)
Internal (over) borrowing	230	232	246	243	228
Less: Reserves and balances	(482)	(419)	(422)	(423)	(435)
Less: Working capital	(273)	(273)	(273)	(273)	(273)
Resources for investments	(755)	(692)	(695)	(696)	(708)
New borrowing or (investments)	(525)	(460)	(449)	(453)	(480)

4.2. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The County Council's current strategy is to maintain borrowing and investments below their underlying levels, known as internal borrowing.

4.3. The Council's CFR is forecast to increase in the current financial year, in particular as the Street Lighting PFI programme continues to be rolled out. The Council's reserves are forecast to remain stable and therefore the current internally borrowed position can be maintained if this continues to be advantageous.

4.4. CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the County Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the County Council expects to comply with this recommendation during 2015/16.

5. Borrowing Strategy

5.1. The County Council currently holds £356 million of loans as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in Table 1 shows that the County Council does not expect to need new borrowing in 2015/16. The County Council may however borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £650 million.

Objectives

5.2. The County Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the County Council's long-term plans change is a secondary objective.

Strategy

5.3. Given the significant cuts to public expenditure and in particular to local government funding, the County Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to use internal resources.

5.4. By doing so, the County Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise.

5.5. In addition, the County Council may borrow short-term loans (normally for up to one month) to cover unexpected cash flow shortages.

Sources

5.6. The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB) and its successor body
- UK local authorities
- any institution approved for investments (see below)

- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except the Hampshire Pension Fund)
- capital market bond investors
- special purpose companies created to enable local authority bond issues

5.7. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- operating and finance leases
- hire purchase
- Private Finance Initiative
- sale and leaseback

5.8. The County Council has previously raised the majority of its long-term borrowing from the PWLB but it continues to investigate other sources of finance, such as local authority loans and bank loans that may be available at more favourable rates.

LOBOs

5.9. The County Council holds £73m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the County Council has the option to either accept the new rate or to repay the loan at no additional cost. In the current low interest rate environment it is unlikely that any lender will exercise their options but there remains an element of refinancing risk. The County Council will take the option to repay LOBO loans at no cost if it has the opportunity to do so.

Short-term and Variable Rate loans

5.10. These loans leave the County Council exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators at section 7 of this strategy.

Debt Rescheduling

5.11. The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The County Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

6. Investment Strategy

6.1. The County Council holds invested funds representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the County Council's investment balance has ranged between £523 and £709 million, and similar levels are expected to be maintained in the forthcoming year.

Objectives

6.2. Both the CIPFA Code and the CLG Guidance require the County Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The County Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

Strategy

6.3. Due to the increasing risk from bank 'bail-ins' and continued low returns from short-term unsecured bank investments, the County Council aims to further diversify into more secure and/or higher yielding asset classes during 2015/16. This is especially the case for the estimated £285m that is available for longer-term investment. The majority of the County Council's surplus cash is currently invested in short-term unsecured bank deposits, certificates of deposit and money market funds. This diversification will therefore represent a substantial change in strategy over the coming year.

Investment Limits

6.4. Given the impact of the Bank Recovery and Resolution Directive, and the recast Deposit Guarantee Schemes Directive, which has increased the credit risk that unsecured bank/building society investments could be 'bailed-in', the following investment limits are proposed to mitigate the risk whilst allowing sufficient flexibility to manage the County Council's investment balances.

6.5. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Maximum limits will also be placed on fund managers and industry sectors as below:

Table 2: Investment Limits	**Cash limit**
Any single organisation, except the UK Central Government	£70m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£70m per group
Any group of pooled funds under the same management	£70m per manager
Registered Providers	£70m in total
Money Market Funds	50% in total

Approved Counterparties

6.6. The County Council may invest its surplus funds with any of the counterparty types in Table 3, subject to the cash limits (per counterparty) and the time limits shown.

Table 3: Approved Investment Counterparties and Limits

Credit Rating	Banks Unsecured	Banks Secured	Government	Corporates	Registered Providers
UK Govt	n/a	n/a	£ Unlimited 30 years	n/a	n/a
AAA	£50m 5 years	£70m 20 years	£70m 30 years	£35m 20 years	£35m 20 years
AA+	£50m 5 years	£70m 10 years	£70m 25 years	£35m 10 years	£35m 10 years
AA	£50m 4 years	£70m 5 years	£70m 15 years	£35m 5 years	£35m 10 years
AA-	£50m 3 years	£70m 4 years	£70m 10 years	£35m 4 years	£35m 10 years
A+	£50m 2 years	£70m 3 years	£35m 5 years	£35m 3 years	£35m 5 years
A	£50m 13 months	£70m 2 years	£35m 5 years	£35m 2 years	£35m 5 years
A-	£50m 6 months	£70m 13 months	£35m 5 years	£35m 13 months	£35m 5 years
BBB+	£20m 100 days	£35m 6 months	£20m 2 years	£20m 6 months	£20m 2 years
BBB or BBB-	£20m next day only	£35m 100 days	n/a	n/a	n/a
None	£35m 6 months	n/a	£35m 25 years	n/a	£35m 5 years
Pooled funds	£70m per fund				

This table must be read in conjunction with the notes below.

Credit Rating

6.7. Investment decisions are made by reference to the lowest published long-term credit rating from Fitch, Moody’s or Standard & Poor’s. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used.

Banks Unsecured

6.8. Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. Unsecured investment with banks rated BBB or BBB- are restricted to overnight deposits at the County Council's current account at NatWest (which is currently rated as BBB+).

Banks Secured

6.9. Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank/building society's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the highest of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank/building society will not exceed the cash limit for secured investments.

Government

6.10. Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 30 years.

Corporates

6.11. Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Investing with any unrated corporate entity will be judged on a case-by-case basis and only considered if suitable security can be obtained for the County Council's investment.

Registered Providers

6.12. Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services, they retain a high likelihood of receiving government support if needed.

Pooled Funds

6.13. Shares in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Money Market Funds that offer same-day liquidity and aim for a constant net asset value will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

6.14. Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the County Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the County Council’s investment objectives will be monitored regularly.

Risk Assessment and Credit Ratings

6.15. Credit ratings are obtained and monitored by the County Council’s treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made,
- any existing investments that can be recalled or sold at no cost will be, and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

6.16. Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as “rating watch negative” or “credit watch negative”) so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Investments targeting higher returns

6.17. As part of the 2014/15 Investment Strategy it was agreed to target £90m for higher yielding investments such as long-term investments with other Local Authorities, or equity, bond or property investments. This amount is in addition to £15m that was identified for long term investments, associated with the Street Lighting PFI. Investments yielding higher returns will contribute additional income to the County Council, although some come with the risk that they may suffer falls in the value of the principle invested.

6.18. The fall in long term interest rates in the current financial year has limited the opportunities that have been available for advantageous long term investments. Of the £105m available the following investments have been made:

Table 4: Higher yielding investments

Type of investments	£m	Average yield
Local Authorities up to 20 years – Street Lighting PFI	15	3.94%
Local Authorities up to 20 years	15	3.83%
Pooled property	10	6.43%*
	40	4.52%
Pooled property (committed not yet called)	15	-
Total investments targeting higher yields	55	-

*year to date total return

6.19. The Director of Corporate Resources' staff with the assistance of the advisors Arlingclose, will continue to look for opportunities to invest the remaining £50m targeting higher returns.

6.20. As shown in Table 4, to date the Council only has one investment where the principal invested is subject to variations in valuation; the £10m invested in a pooled property fund. This investment has been initially successful, as at 31 December the investment was valued at £10.34m and has returned £0.31m in dividends. It is recommended that these initial returns are used to create a reserve of £0.5m in the County Council's accounts as protection against the irrecoverable fall in value of any investments. This is prudent given the additional risk that is being taken in targeting investments with higher returns.

Other Information on the Security of Investments

6.21. The County Council understands that credit ratings are good but not perfect predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

6.22. Based on the available information and the advice of the County Council's advisers, Arlingclose, the Director of Corporate Resources may reduce the investment limits shown in Tables 2 and 3, and suspend investing with certain counterparties as necessary.

6.23. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the County Council's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

Specified Investments

6.24. The CLG Guidance defines specified investments as those:

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement,
- not defined as capital expenditure by legislation, and
- invested with one of:
  - the UK Government,
  - a UK local authority, parish council or community council, or
  - a body or investment scheme of "high credit quality".

6.25. The County Council defines "high credit quality" organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds "high credit quality" is defined as those having a credit rating of A- or higher.

Non-specified Investments

6.26. Any investment not meeting the definition of a specified investment is classed as non-specified. The County Council does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, (i.e. those that are due to mature 12 months or longer from the date of arrangement), pooled funds that the County Council intends to hold as long-term investments (for more than a year) and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in Table 5 below.

Table 5: Non-Specified Investment Limits

	Cash limit
Total long-term investments	£285m
Total investments without credit ratings or rated below A- (excluding investments with other local authorities)	£190m
Total non-Sterling investments	£0m
Total investments in foreign countries rated below AA+	£0m
Total non-specified investments	£475m

Liquidity Management

6.27. The County Council has due regard for its future cash flows when determining the maximum period for which funds may prudently be committed. Historic cash flows are analysed in addition to significant future cash movements, such as payroll, grant income and council tax precept. Limits on long-term investments are set by reference to the County Council's medium term financial position (summarised in Table 1) and forecast short-term balances.

7. Treasury Management Indicators

7.1. The County Council measures and manages its exposures to treasury management risks using the following indicators.

Interest Rate Exposures

7.2. This indicator is set to control the County Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the amount of principal borrowed or invested will be:

	2015/16	2016/17	2017/18
Upper limit on fixed interest rate investment exposure	£285m	£250m	£250m
Upper limit on variable interest rate investment exposure	£800m	£800m	£800m
Upper limit on fixed interest rate borrowing exposure	£800m	£780m	£740m
Upper limit on variable interest rate borrowing exposure	£800m	£780m	£740m

7.3. Fixed rate investments and borrowings are those where the rate of interest is fixed for the whole financial year. Short-term instruments (with a maturity of less than one year) are classed as variable rate.

Maturity Structure of Borrowing

7.4. This indicator is set to control the County Council’s exposure to refinancing risk. The upper and lower limits on the maturity structure of fixed rate borrowing will be:

	Upper	Lower
Under 12 months	50%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	75%	0%
10 years and within 20 years	75%	0%
20 years and within 30 years	75%	0%
30 years and above	100%	0%

7.5. Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

Principal Sums Invested for Periods Longer than 364 days

7.6. The purpose of this indicator is to control the County Council’s exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total principal sum invested to final maturities beyond the period end will be:

	2015/16	2016/17	2017/18
Limit on principal invested beyond 364 days	£285m	£250m	£250m

8. Other Items

8.1. There are a number of additional items that the County Council is obliged by CIPFA or DCLG to include in its Treasury Management Strategy.

Policy on Use of Financial Derivatives

8.2. Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities’ use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

8.3. The County Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the County Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

8.4. Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit. The use of financial derivatives is not planned as part of the implementation of the Treasury Management Strategy and any changes to this would be reported to members in the first instance.

Investment Training

8.5. The needs of the County Council's treasury management staff for training in investment management are assessed annually as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change.

8.6. Staff regularly attend training courses, seminars and conferences provided by Arlingclose and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA and other appropriate organisations.

8.7. CIPFA's Code of Practice requires that the Council ensures that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. All County Council members were invited to a workshop presented by Arlingclose on 28 November 2014, which gave an update on treasury matters.

Investment Advisers

8.8. The County Council has appointed Arlingclose Limited as treasury management advisers and receives specific advice on investment, debt and capital finance issues. The quality of this service is controlled through quarterly review meetings with the Director of Corporate Resources and her staff and Arlingclose.

Investment of Money Borrowed in Advance of Need

8.9. The County Council may, from time to time, borrow in advance of need, where this is expected to provide the best long term value for money. Since amounts borrowed will be invested until spent, the County Council is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the County Council's overall management of its treasury risks. The total amount borrowed will not exceed the authorised borrowing limit of £650 million.

Appendix A – Arlingclose Economic & Interest Rate Forecast January 2015

Forecast:

- We continue to forecast the first rise in official interest rates in Q3 2015, but the risks to this forecast are very much weighted to the downside. The February Inflation Report will be key to our review of the possible path for Bank Rate.
- We project a slow rise in Bank Rate. The pace of interest rate rises will be gradual and the extent of rises limited; we believe the normalised level of Bank Rate post-crisis to range between 2.5% and 3.5%.
- Market sentiment (derived from forward curves) has shifted significantly lower in the past three months; market expectations are now for a later increase in interest rates and a more muted increase in gilt yields.
- The short run path for gilt yields has flattened due to the sharp decline in inflation expectations. We project gilt yields on an upward path in the medium term.
- The short run path for gilt yields is flatter due to the deteriorating Eurozone situation. We project gilt yields on an upward path in the medium term.

	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18
Official Bank Rate													
Upside risk				0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Arlingclose Central Case	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50	1.75	1.75	1.75
Downside risk			0.25	0.25	0.50	0.50	0.75	0.75	1.00	1.00	1.00	1.00	1.00
3-month LIBID rate													
Upside risk	0.10	0.20	0.20	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30
Arlingclose Central Case	0.55	0.60	0.80	0.90	1.05	1.15	1.30	1.40	1.55	1.65	1.80	1.95	2.00
Downside risk	0.15	0.20	0.30	0.40	0.55	0.65	0.75	0.85	0.95	0.95	0.95	0.95	1.00
1-yr LIBID rate													
Upside risk	0.10	0.20	0.20	0.30	0.30	0.30	0.30	0.30	0.40	0.40	0.40	0.40	0.40
Arlingclose Central Case	0.95	1.00	1.20	1.30	1.45	1.55	1.70	1.80	1.95	2.05	2.20	2.35	2.40
Downside risk	0.15	0.20	0.30	0.50	0.55	0.60	0.65	0.70	0.75	0.80	0.80	0.80	0.80
5-yr gilt yield													
Upside risk	0.35	0.40	0.40	0.40	0.40	0.40	0.40	0.45	0.45	0.45	0.45	0.50	0.50
Arlingclose Central Case	1.10	1.20	1.30	1.40	1.50	1.65	1.80	1.95	2.10	2.20	2.35	2.40	2.50
Downside risk	0.35	0.35	0.40	0.45	0.50	0.50	0.55	0.60	0.65	0.70	0.70	0.70	0.75
10-yr gilt yield													
Upside risk	0.35	0.40	0.40	0.40	0.40	0.45	0.45	0.45	0.45	0.50	0.50	0.55	0.55
Arlingclose Central Case	1.60	1.70	1.80	1.90	2.00	2.15	2.30	2.45	2.60	2.70	2.85	2.90	3.00
Downside risk	0.35	0.35	0.40	0.45	0.50	0.50	0.55	0.60	0.65	0.70	0.70	0.75	0.80
20-yr gilt yield													
Upside risk	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55	0.55
Arlingclose Central Case	2.10	2.20	2.30	2.35	2.45	2.50	2.65	2.75	2.90	3.00	3.15	3.20	3.30
Downside risk	0.35	0.40	0.50	0.60	0.70	0.75	0.75	0.75	0.80	0.85	0.85	0.90	0.90
50-yr gilt yield													
Upside risk	0.35	0.40	0.45	0.50	0.50	0.50	0.50	0.50	0.50	0.55	0.55	0.55	0.55
Arlingclose Central Case	2.15	2.25	2.35	2.40	2.50	2.55	2.70	2.80	2.95	3.05	3.20	3.25	3.35
Downside risk	0.35	0.40	0.50	0.60	0.70	0.75	0.75	0.75	0.80	0.85	0.85	0.90	0.90

Appendix B – Existing Investment & Debt Portfolio Position

	31.12.2014 Actual Portfolio £m	31.12.2014 Average Rate %
External Borrowing:		
PWLB – Fixed Rate	283	
Other Loans	73	
Total External Borrowing	**356**	**4.92**
Other Long Term Liabilities:		
Street Lighting PFI	120	
Waste Management Contract	65	
Total Gross External Debt	**541**	**-**
Investments:		
Direct Deposits		
- Barclays	50	
- Close Brothers	15	
- HSBC	50	
- Lloyds	55	
- Nationwide	40	
	210	**0.90**
Certificates of deposit		
- Deutsche Bank	29	
- Nordea	15	
- Rabobank	15	
- Standard Chartered	50	
	109	**0.77**
Money Market Funds		
- Ignis	**19**	**0.47**
Other Local Authorities	**162**	**1.71**
Higher yielding investments		
- CCLA Property Fund	10	
- Other Local Authorities	30	
	40	**4.52**
Total Investments	**540**	**1.37**
Net Borrowing	**1**	**-**

Appendix C - Prudential Indicators 2015/16

The Local Government Act 2003 requires the County Council to have regard to the Chartered Institute of Public Finance and Accountancy's Prudential Code for Capital Finance in Local Authorities (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the County Council has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

Estimates of Capital Expenditure

The County Council's planned capital expenditure and financing may be summarised as follows.

Capital Expenditure and Financing	2014/15 Revised £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
Total Expenditure	**265**	**236**	**168**	**159**
Capital receipts	11	16	5	2
Grants and other income	147	120	114	141
Revenue contributions	36	68	35	16
Contributions from reserves	28	6	1	2
Total Financing	**222**	**210**	**155**	**161**
Supported borrowing	0	0	0	0
Prudential borrowing	17	31	24	11
Less repayments from capital receipts etc	(6)	(5)	(11)	(13)
Finance lease	32	0	0	0
Total Funding	**43**	**26**	**13**	**(2)**
Total Financing and Funding	**265**	**236**	**168**	**159**

Estimates of Capital Financing Requirement

The Capital Financing Requirement (CFR) measures the County Council's underlying need to borrow for a capital purpose.

Capital Financing Requirement	31.03.15 Revised £m	31.03.16 Estimate £m	31.03.17 Estimate £m	31.03.18 Estimate £m
Total CFR	**771**	**765**	**741**	**702**

The CFR is forecast to fall over the next three years as capital expenditure financed by debt is outweighed by resources put aside for debt repayment.

Gross Debt and the Capital Financing Requirement

In order to ensure that over the medium term debt will only be for a capital purpose, the County Council should ensure that debt 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. This is a key indicator of prudence.

Debt	31.03.15 Revised £m	31.03.16 Estimate £m	31.03.17 Estimate £m	31.03.18 Estimate £m
Borrowing	354	343	330	316
PFI liabilities	185	176	168	158
Total Debt	**539**	**519**	**498**	**474**

Total debt is expected to equal or remain below the CFR during the forecast period.

Operational Boundary for External Debt

The operational boundary is based on the County Council's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the County Council's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring. Other long-term liabilities comprise finance lease, Private Finance Initiative and other liabilities that are not borrowing but form part of the County Council's debt.

Operational Boundary	2014/15 Revised £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
Borrowing	620	620	610	580
Other long-term liabilities	190	180	170	160
Total Debt	**810**	**800**	**780**	**740**

Authorised Limit for External Debt

The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the County Council can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

Authorised Limit	2014/15 Revised £m	2015/16 Estimate £m	2016/17 Estimate £m	2017/18 Estimate £m
Borrowing	640	650	630	600
Other long-term liabilities	240	220	210	200
Total Debt	**880**	**870**	**840**	**800**

Ratio of Financing Costs to Net Revenue Stream

This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

Ratio of Financing Costs to Net Revenue Stream	2014/15 Revised %	2015/16 Estimate %	2016/17 Estimate %	2017/18 Estimate %
General Fund	7.14%	6.99%	6.92%	6.78%

Incremental Impact of Capital Investment Decisions

This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax levels. The incremental impact is the difference between the total revenue budget requirement of the current approved capital programme and the revenue budget requirement arising from the capital programme proposed earlier in this report.

Incremental Impact of Capital Investment Decisions	2015/16 Estimate £	2016/17 Estimate £	2017/18 Estimate £
General Fund - increase in annual band D Council Tax	£2.06	£5.44	£3.44

Adoption of the CIPFA Treasury Management Code

The County Council adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition in February 2012.

Appendix D – Annual Minimum Revenue Provision Statement 2015/16

Where the County Council finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the County Council to have regard to the Department for Communities and Local Government's Guidance on Minimum Revenue Provision (the DCLG Guidance) most recently issued in 2012.

The broad aim of the DCLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

The DCLG Guidance requires the County Council to approve an Annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP. The four MRP options available are:

- Option 1: Regulatory Method
- Option 2: CFR Method
- Option 3: Asset Life method
- Option 4: Depreciation Method

MRP in 2015/16: Options 1 and 2 may be used only for supported (i.e. financing costs deemed to be supported through Revenue Support Grant from Central Government) capital expenditure funded from borrowing. Methods of making prudent provision from unsupported capital expenditure include Options 3 and 4 (which may also be used for supported capital expenditure if the County Council chooses.

The County Council will apply Option 1/Option 2 in respect of supported capital expenditure funded from borrowing and Option 3/Option 4 in respect of unsupported capital expenditure funded from borrowing.

MRP in respect of leases and Private Finance Initiative schemes brought on Balance Sheet under the International Financial Reporting Standards (IFRS) based Accounting Code of Practice will match the annual principal repayment for the associated deferred liability.

Capital expenditure incurred during 2015/16 will not be subject to a MRP charge until 2016/17.

Consultation Responses

A consultation paper on the County Council's budget proposals for 2015/16 was produced and submitted to the Hampshire Chamber of Commerce in December 2014. The paper acknowledged the status of the 2015/16 budget in that key decisions in respect of savings proposals had already been taken by the County Council in February 2014, in order to provide the time and capacity for the savings to be fully implemented by April 2015.

The paper was circulated to all of the key members and committees of the Hampshire Chamber of Commerce and detailed below is the general feedback that was received:

- The Hampshire Chamber of Commerce (The Chamber) recognises the current financial of the County Council in respect to having to respond to Government grant reductions over a sustained period.
- The Chamber acknowledges that fact that there is little to comment on for the setting of the 2015/16 budget given that key decisions around savings proposals were already agreed in February 2014.
- Issues around transport, access to superfast broadband and the role that the County Council can play in economic development are all things which are very high on the business community agenda.
- The Chamber is aware that the Transformation to 2017 Programme is currently being developed and it looks forward to being able to contribute towards the future consultation exercises that are planned.