14 February 2024	ITEM: 6

Extraordinary Corporate Overview and Scrutiny Committee

Medium Term Financial Strategy 2024/25

Wards and communities affected:	**Key Decision:**
All	Key

Report of: Cllr G Snell – Finance, Human Resources and Payroll

Accountable Director: Steven Mair, Interim Chief Financial Officer/s151

This report is Public

Version: Final

1. Executive Summary

1.1. The Council's financial position is virtually unprecedently challenging and will remain so for several years.

1.2. Nonetheless the position is forecast to improve considerably in the next 5 years, via the divestment of assets, the implementation of a challenging savings programme, working differently and service delivery changes .

1.3. The three key financial indicators* reflecting this are shown below:

Table 1 – Key Financial Indicators

Financial Indicators / Movement	***General Fund Debt @3.5%**	Cost of Debt - MRP and Interest	***Cost of Debt as % of Revenue Budget**	***Capitalisation Direction**
	£m	£m	**%**	**£m**
2023/24 Opening Budget	1,292.50	155.84	105.9%	180.2
2023/24 Movement	-858.50	48.05	32.6%	54.4
2023/24 Closing Forecast	434.00	203.89	138.5%	234.6
2028/29 Forecast	314.26	44.50	24.8%	24.1
Improvement 2023/24 Opening Budget to 2028/29	**-978.24**	**-111.34**	**-81.1%**	**-156.0**
Improvement required to reach Ultimate Target		26.60	14.85%	24.1
Ultimate Target for Council		17.90	9.99%	0.0

Version Control (delete as appropriate)
Version 1 - First draft ready for DMT, SLT and Commissioner input; **Version 2** - Second Draft ready for Portfolio Holder, Leader and other Member Input; **Version 3** - Third draft for any further comments; **Version Committee** – Draft ready for submission to public committee; **Version Cabinet** – Final version ready for Cabinet/Executive decision

1.4. The General Fund Debt has decreased in 2023/24 and is expected to continue to improve to 2028/29.

1.5. The Cost of Debt is the General Fund Debt interest cost and the MRP charge, has increased in 2023/24 due to the recent legal ruling that historic MRP must be charged to current and future years. This cost of debt / revenue ratio improves by 2024/25 but is still above the ultimate target of below 10%.

1.6. The Capitalisation Directive again increases in 2023/24, due to the MRP charge, but reduces dramatically by 2028/29.

1.7. This obviously depends on the achievement of a number of key financial deliverables:

- sale of investments generating the maximum possible value by 2027/28;
- a capital programme that has for five years an average of £1m per annum general funded expenditure;
- sale of over £100m of capital property assets by 2027/28;
- revenue savings in 2024/25 of £18.2m plus further savings and reduced growth of £1.7m to offset the reduced income from a 7.99% Council Tax increase against one of 9.99%
- revenue savings in 2025/26 of £18.2m and savings of £13.6m in 2026/27, 2027/28 and 2028/29.

1.8. If any of the targets above are not realised, alternative savings to the same value and timelines need to be delivered, otherwise the financial position of the council will worsen. This includes additional in-year pressures that have not been forecast in the MTFS.

1.9. A wide range of improvements in financial management are required, some are in progress, others are planned and need to be addressed along with an overarching need for a change programme to ensure consistent innovative high quality financial services.

1.10. By delivering all of the above the financial directions will be addressed and the financial position of the Council can improve. The finance service will support the change of the Council to its Enabling Model, which is focused on innovating and taking different approaches, collaborating with partners and politicians to deliver value for money, local services required by residents and business; whilst remaining affordable in the medium and long term.

1.11. These initiatives taken together have the potential to enable the Council to achieve financial stability

Recommendation(s)

1.12. It is recommended that the Committee comment on the Medium Term Financial Strategy (MTFS) and in doing so review:

- the financial targets summarised in paragraph 1.3,
- the financial assumptions / deliverables as summarised at paragraph 1.4 to 1.7;

- that if any of the above targets or assumptions adversely vary, alternatives to the same timescale and value will need to be identified and implemented.

2. Commissioners' comments

2.1 To be added as an addendum prior to the meeting.

3. Introduction and Background

3.1. The Councils original Medium-Term Financial Strategy (MTFS) 2023/24 to 2025/26 was presented to Cabinet on 22 February 2023, and subsequently approved by Full Council on 1 March 2023.

3.2. This report resets the MTFS for the period 2024/25 to 2028/29, as part of the budget setting process and provides a 10 year estimate of the Council's position back to 2018/19 (consolidated value). Thus allowing for the period since the impact of the Council's financial investments.

4. Issues, Options and Analysis of Options

Issues

4.1. There are four direct and indirect financial drivers for the MTFS:

- the virtually unprecedented financial position the Council faces,
- Government Directions and Related Reports,
- the changes to the Council's operating model and approach,
- the need to improve the financial management of the Council.

4.2. From the financial perspective these drivers are aimed at securing a financially sustainable future for the Council, with three key indicators, identified at Table 1:

- the Council's General Fund Debt Cost, being reduced to an ultimate target of £17.9m, based on an estimated interest rate of 3.5%;
- debt payments as a proportion of the Council's budget are less than 10%,
- the Extraordinary Financial Support I.e. Capitalisation Direction that the Council has to rely on, is reduced to £0/a balanced annual revenue budget.

4.3. This will take a considerable period of time, change and action and the first medium term review point is 2028/29. The Council will not be financially sustainable before then and is predicted to require continued support after 2028/29.

Financial Position

4.4. In December 2022 the Council faced[1]

- a deficit in annual revenue investment income budget of £41.5m;

[1] Financial Update - Quarter 2 2022-23.pdf (thurrock.gov.uk)

- a collapse in asset values of investments;
- inaccessibility to the short-term local authority borrowing market and rising interest rates resulting in the need to transfer £1,035m to PWLB and interest rates rising from 0.5% to 5% at an increased annual cost of £28.3m in 2023/24;
- a then estimated budget pressure of £116m to budget for MRP;
- a potential long term Capitalisation Direction of £1,042m;
- continual revenue budget deficits for the long-term

4.5. The overall financial challenge fundamentally arose from:

- over-reliance on investments to support revenue - proportion risk;
- over investment in one solar/windfarm basket - investment concentration risk;
- long-term investments funded by borrowing on temporary markets from other local authorities - interest risk;
- very significantly inadequate budgeting for MRP - legality risk;
- inadequate levels of previous revenue savings – unsustainability risk;
- an excessive capital programme – affordability risk.

Government Directions and Related Reports

4.6. The Council received Directions from the Secretary of State which are set out in Appendix 1 and are elements of Part 1 of the Local Government Act 1999, combined with five specific actions.

4.7. The Council also received on 15 June 2023 the Best Value Inspection Report. Without pre-empting what the Council's external auditors may report in the future, it is reasonable to assume they will make recommendations in respect of the accounts and possibly other matters.

4.8. Both of these have to be addressed, as will any future audit recommendations.

Council Operating Model

4.9. The Council has previously provided a level of direct service in a manner and quantum that it will not be able to sustain in the future. Issues that will be addressed include:

- silo and traditional working;
- continuous improvement and appropriate ambition;
- working at pace and working with partners.

4.10. The challenge for the Council is difficult, to rebuild confidence across government, partners stakeholder and those who live and work in the borough. Part of this journey is building financial sustainability in the immediate and medium term, demonstrating it can confidently manage its resources and services whilst delivering value for money.

4.11. The new operating model requires all involved to change, deliver innovation and take different approaches to service delivery and council operations. The Council will continue its transparent approach, moving to an Enabling Council (commissioning services), collaborating with partners, service users, community groups and seeking new ways of delivery that serve the businesses and residents, sharing the responsibilities and setting a financially balanced budget.

4.12. Council values focus on behavioural drivers that are consistent, create impact and use less resources:

- accountability
- integrity
- collaborative
- impactful
- responsiveness
- adaptability

4.13. The new operating model focuses on affordable and responsive services, use digital tools for enablement, harness strengths of partners, be a provider of last resort. To do this we need our partnerships deliver value for money and social value for all commissioned services.

4.14. Significant change is already happening and with the support of the Commissioners and DLUCH, we have already started our transformation, developing saving and growth opportunities across our services for the next 5 years. The Council needs to become more effective and efficient, developing and modifying corporate plans, finance reporting and governance.

4.15. The Council has 4 major streams of budget challenges which are underway:

- selling £1.035bn of investments to the fullest extent possible (to be determined) to pay down debt,
- generating over £100m of capital receipts from property to pay down debt,
- reducing reliance on borrowing to fund the general fund capital programme to avoid increasing debt,
- saving £18.2m from the revenue budget for next 2 years and a further £13.65m for each of the following 3 years.

4.16. These budget challenges will require a locality approach that maximises local assets and drives outcomes through value driven partnerships. A focus on early intervention and preventative services savings targets will require the council to change the way it delivers its services, collaborates with partners and addresses increasing demand. This is part of the council changing to an Enabling Council.

Financial Management

4.17. An update on all actions is shown in the remainder of the report, starting and focussing on those being undertaken to generate financial savings, followed in brief summary, for the government directions, operating model and financial management.

Actions to Address the Issues

4.18. The following actions are key to addressing the financial position:

- sale of investments generating the maximum possible value by 2027/28;
- a capital programme that has for five years an average of £1m per annum general funded expenditure;
- sale of over £100m of capital property assets by 2027/28;
- revenue savings in 2024/25 of £18.2m plus further savings and reduced growth of £1.7m to offset the reduced income from a 7.99% Council Tax increase against one of 9.99%
- revenue savings in 2025/26 of £18.2m and savings of £13.6m in 2026/27, 2027/28 and 2028/29.

5. Divesting the Council's Investments

5.1. The aim of this workstream is sell £1.035bn of investments to the fullest extent possible and pay down debt and in doing so ensure the governance, project management, budgetary control etc of this programme of work is properly undertaken. This is the single major cause of the Council's financial problems and the single major solution to resolving this.

5.2. In recent years, the Council had built up a substantial investment portfolio, all funded by borrowing via temporary loans from other local authorities. Not only is it necessary to divest from the investments to satisfy the Government Directions, but also because the costs of funding the portfolio have risen significantly in the past 18-24 months which combined with proper accounting for MRP means that none of the investments are generating a positive yield for the Council. Furthermore, the medium-term interest rate forecasts indicate that rates are unlikely to reduce markedly in the medium-term. Consequently, it is imperative to divest to reduce the financial risk associated with the portfolio. Notwithstanding this, the Council also needs to ensure that best value judgements are taken in respect of the disposal of each investment.

5.3. The Council's investment portfolio pre commencement of the divestment strategy comprised 14 investments totalling £1.035 billion. The strategy to date has focussed on recovering the largest investments by value, including Toucan, JLG/JCF, PWE, CCLA and the two Wind Farms. Recovery plans for each of these investments are well progressed.

5.4. Collectively these positions represent circa 93% (based on original book values), therefore, a significant % of the investment exposure is due to be reduced over the near term. Divestment analysis has also commenced on three of the tail investments, which collectively represent a further c.4% of the Council's investment portfolio. Preliminary analysis has commenced on the remaining positions, comprising 3% of the portfolio, with more detailed analysis due to commence in Quarter 1 2024.

5.5. Via the support of the Council's advisors, Toucan and JLG/JCF have specifically designed recovery strategies implemented. Both companies are currently in administration, supported by the Council, and they are in the process of realising returns to the Council. To date, approximately £107m of cash proceeds have been recovered and returned to the Council as shown in Table 2 at paragraph 5.14. The Council is forecast to receive a further c.

£93.4[2] million from CCLA on or around the 5th of February. The Council is expected to receive c. £436[3] million from Toucan during February 2024. Therefore, in total, the Council is forecast to have recovered £633mn in cash proceeds by the end of February.

Key Financial Issues

5.6. The majority of the investment portfolio meets the statutory definition of capital expenditure and should have had MRP charged. The CCLA Property Fund and some of the solar farm investments do not meet the statutory definition of capital expenditure, but were nonetheless financed from borrowing, and therefore require the accounts to be restated.

5.7. The MRP on both the capital investments and the Capitalisation Direction is at least 5%. Interest rate costs are now running at c. 7%. Consequently, the overall cost of holding the investments is at least 12%. In all cases investment returns are below 12% or expected to be so, given current known information. Therefore, even where there were regular Local Government Treasury Management operations, an authority would look to divest of those “loss making” investments, providing that there is no significant financial downside to the divestments or repaying the borrowings.

5.8. The actual interest and MRP percentages may vary depending on the useful life of the asset and the actual interest rate at a point in time, however as a guide 12% is a reasonable indicator which will be refined for each specific instance.

5.9. Thus the Council has adopted an indicative hurdle rate of 12% (i.e.7% PWLB rate and 5% MRP) is set for investment yield / return, with anything yielding less being put forward for sale, subject to the detail of the individual investment, the Council’s contractual obligations and the ability to manage any associated risk.

5.10. In addition, the Council did not have the skills or capacity to manage these investments when it first entered into them, which is contrary to the Statutory Guidance on Local Government Investments and its status as a MiFID II professional investor. Furthermore, it is only currently able to manage the current portfolio with substantial external advisory support.

5.11. There was very limited investment portfolio monitoring and reporting back to Members, despite the size of the Council’s investment portfolio (just over £1billion) being equivalent to, for example, a London borough pension fund for which regular (i.e. quarterly) investment performance monitoring against benchmark performance measures is a requirement, together with independent investment advice. In contrast there was no such detailed performance monitoring or independent investment advice sought or provided. This is now being addressed.

Progress

[2] The value is crystalised at the end of the month, planned to be early 2024. Therefore, the remains exposure to price movements.

[3] Remains subject to contract, with potential price exposure. This is expected to be finalised by the time of releasing this report.

5.12. The current work in progress on recovery of funds is shown below, at an overall level (on an original book value basis) the Council is progressing well, as shown below:

Cash recovered to date	10% of portfolio, (from a combination of the investments, including 1 fully exited)
In process of divestment	81% of portfolio (5 investments, plus 1 investment fully divested)
Options/divestment analysis underway	4% of portfolio (2 investments)
Preliminary reviews underway	3% of portfolio (4 investments)
Restructured	2% of portfolio (1 investment)

5.13. It is important to note that the Council has some tail positions which in the main are small, illiquid positions. In certain cases, the Council's exit is dependent on the company's ability to realise value from the assets on their balance sheet, or to access a refinancing. This includes the tail investment positions which are fund structures investing in small to medium sized companies. Due to the increased cost of capital, driven by the increase in the interest rates, access to refinancing has generally reduced. In the context of the Council's portfolio, the tail positions also represent a much smaller residual exposure once the above key positions have all been worked through.

5.14. In the short term the following funds have been or should be received by 31 March 2024. This includes distributions arising from the sale of the Toucan asset portfolio.

Table 2 – Funds expected to be received by 31 March 2024

Investment	Expected Funds	Explanation
	£m	
Toucan		
Cash Received to Date	73.60	Cash distributions received to date
Cash Expected in Feb 2024	436.00	Forecast to be received in February 2024, subject to contract.
Pure World Energy (PWE)	11.30	Repayment of funds and distribution
Fund Investment	10.00	Cash returned following end of relationship agreement
Just Loans Group (JLG) / Just Cash Flow (JCF)		
Cash Received to Date	10.00	Cash distributions received to date. Further amounts are expected over the coming 18 months.
CCLA		
Cash Received to Date	0.90	Cash from redemption of Diversified Income Fund
Cash Expected in Feb 2024	91.50	Forecast from redemption of the CCLA Property Fund, subject to price movement.
Total	**633.30**	

The receipts are used to reduce the Capitalisation Direction requirement and offset the investment revenue debt

Toucan

5.15. Toucan Energy Holdings 1 (TEH1) is the most significant investment in the Council's portfolio representing more than 60% of the Council's investment portfolio. Administrators from Interpath Advisory were appointed in November 2022 and have prepared the assets (the solar portfolio) for sale, alongside their advisors, the Council and its advisors. Following a competitive global sales process, a preferred buyer has now been selected and the sale completed on 21st January 2024.

5.16. There are a wide range of potential litigation claims in relation to the Toucan investment and the Council may be able to recover further monies via this route. This is a complex matter and is unlikely to be a quick process. The Council will need to decide, together with Interpath (the Administrators), which claims are best to pursue in the first instance, given the common pool of assets being targeted. The Council is close to concluding pre-action work and the next phase of work, following the sale of Toucan, will be to undertake a cost-benefit analysis to determine those claims with the strongest chances of success and ensure that these are pursued in the first instance.

JLG/JCF

5.17. The Council has several bond investments totalling an original investment amount of £3.6m in Just Loans Group (JLG) and Just Cash Flow (JCF), affiliated companies which make loans to UK SMEs. Most of the loans are small, with the average loan size being circa £60k, but there are also a number of larger loans above £1m. JLG defaulted on one bond tranche in May 2021 and subsequent investigation revealed wider issues within the group and concerns for the Council's investments. Given the fundamental nature of the risks, significant work was undertaken by the Council and its advisors to stabilise the Group and prevent a disorderly collapse, which would have been more financially damaging for the Council. A restructuring and insolvency process was undertaken, and the loans are currently being serviced and recovered by the administrator and an external servicer. To date, the collection of the underlying loans has significantly improved, with net proceeds being distributed to back to investors on a regular basis.

5.18. The Council is expected to receive net recoveries over the next 18 months. Part of this has already begun to come through, with the Council having received c. £11m to date.

CCLA

5.19. The Council had invested in to two pooled funds run by CCLA (Churches, Charities and Local Authorities) Investment Management Limited, a well-known investment manager for local authorities. The majority of the exposure – the investment of £93.4m – is in the CCLA Local Authorities' Property Fund (LAPF), which invests into a long-term, actively managed, and diversified portfolio of UK commercial property. There was also a small investment of £1m in the Diversified Income Fund, which looks to generate an income-focused return through a diversified actively managed portfolio of stocks, bonds, cash, and infrastructure assets in the main.

5.20. As of January 2024, the £103m is now valued at £92m Disposal of this investment was confirmed by the Council in July 2023, with redemption proceeds expected to be received early February 2024.

5.21. CCLA have confirmed that they have maintained significant cash in the fund, giving comfort that the redemption notice period should be met. The redemption proceeds are due in the first week of February 2024.

5.22. The divestment of the CCLA Diversified Income Fund has been completed and the proceeds have been received.

Wind Farms

5.23. The Council has invested in two wind farms which are both illiquid private investments.

5.24. The Council's advisors have been analysing the assets as well as mapping out options for the Council and key dependencies. Both wind farms assets appear to be performing well and will be sold by a competitive sales process. Potential sales agents have been approached and following a procurement exercise in February, a sales agent will be selected to market and sell the investments

5.25. Offers will be evaluated, and following an options appraisal and best value assessment, a preferred buyer will be selected. Sales proceeds are expected to be received in the first half of 24/25.

Tail Investment – Credit Fund

5.26. The Council is an investor in a private credit fund, which makes loans to small-medium-sized companies. The Council invested in both the fund as well as co-invested alongside it to make loans to specific companies. £10m has been divested to date from the original exposure of £24.3m. A detailed options analysis paper is currently being prepared and due to be shared with the Council by the end of March 2024.The fund is illiquid, and the terms do not allow for divestment before maturity, outside of a secondary sale. The Fund is due to winddown over the next couple of years, with returns distributed to investors over this period. Due to weakness in the economy, the fund's manager is sensitive to ensuring that the underlying positions are managed accordingly, seeking to mitigate risks and optimise exits.

Tail Investment - Pure World Energy Ltd (PWE)

5.27. PWE is a company supplying heat pumps to council-owned leisure centres in the main which the Council invested £30m in. It has since been restructured after an options-based appraisal by Council. The majority of debt was converted to equity and £2m of senior debt retained currently. £10m has been recovered in cash and approximately £1.25m of debt repayments paid to date. The business has appointed two non-executive directors, to add an additional layer of governance and strategic input. The company is currently finessing its business plan, seeking to increase value to shareholders. The non-executive directors are implementing reporting mechanisms, designed to report to the Council on a periodic basis.

Tail Investment – Social Housing Developer

5.28. The Council has a loan to a provider and developer of care homes, assisted living accommodation and sheltered housing to local authorities. The Company has completed several projects to date, with further properties under construction. Due to weakness in the economy and other factors, the position requires a managed exit plan. The company and the Council are currently in discussions to exit the position.

5.29. An options analysis is currently being prepared on the position, examining the state of the business and potential options available to exit.

Tail Investment – Other

5.30. For the remaining tail investments, preliminary analysis, and information gathering is underway. The goal is to undertake preliminary analysis in the next 3 months with full options analysis being completed periodically over the coming 3-6 months in order of priority and materiality. A process has been agreed for all positions, which will comprise the following:

preliminary review: initial assessment, views on liquidity availability and options being explored. Interim updates will be provided, with positions worked through in an orderly fashion in order of materiality;

post initial assessment, officers will decide on priorities and areas of focus, and authorise work to be progressed on options. They will also identify any decisions and map out timelines, governance, and review requirements. Lastly, they will ascertain any impacts on divestment timelines and wider considerations, e.g., borrowings / MRP;

in advance of decisions, a detailed analysis will be prepared examining options; assessment of position value; contractual obligations / limitations; any early divestment options; and recommendations for next steps;

decision options will then be presented to members and the chosen options will then be implemented.

Divestment Strategy

5.31. The divestment strategy being pursued by the Council involves complex financial and legal issues and it has been vital that the Council is in receipt of high-quality and relevant financial and legal advice to support decision-making and protect the Council's investment. The complexity of the investments and remediation work undertaken has been significant and is both a function of the size of the assets as well as deeper underlying issues that were uncovered, which required significant resources to remedy. For example, in the case of Toucan, legal uncertainties as well as the opacity of cashflows and the use of the Council's proceeds necessitated significant work on valuations, forensic investigations, tracing of assets, resolution of complex financial structures and deep dive due diligence. Similarly, in the case of JLG, the complexity of the loan book coupled with multiple creditors and poor management required significant analysis, restructuring of the company, resolution of identified security issues and implementation of controls

5.32. In addition, due to Toucan and JLG/JCF being in administration, the Council has required significant legal and financial support to advise on the administrations to realise distributions for the Council. A separate paper has been produced on fees

5.33. The total advisor costs including the administrators' direct costs, administrators' advisor costs and the Council's own advisor costs as at July 2023 are estimated at £17.4m to date with forecast additional costs of £29.1m. These costs are under review and may change.

Depending on the specifics of the investigations and legal actions undertaken by the Council and the administrators, these costs may be smaller or larger, though the Council will conduct cost-benefit analysis to understand all costs and limit extraneous costs.

5.34. The Council is very mindful of the responsibilities of those outside of the Council for the situation the Council finds itself in and proactive work is being instigated in respect of potential remedies against individuals and organisations who may not have met the standards expected of them.

5.35. Where opportunities present themselves to make recoveries through litigation all necessary action will be taken subject to securing the necessary legal advice on the merits of a potential claim and the undertaking of a cost benefit analysis.

5.36. The current position is that the Council is close to concluding the pre-action process on all claims which have been identified to date and decisions will need to be taken in the near future on whether those claims are viable and whether proceedings should be issued.

6. Capital Programme

6.1. The aim for the capital programme is to meet the requirements of the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code, which requires local authorities to produce a Capital Programme to demonstrate how capital expenditure, capital financing and treasury management activity contribute to the provision of planned outcomes and take account of stewardship, value for money, prudence, sustainability and affordability. As the Council is unable to borrow for anything other than refinancing debt, the fundamental aim is to reduce general fund borrowing to a nil borrowing requirement.

6.2. The preparation of the capital programme has included:

- a review of the previously approved programme to establish the base line;
- reviews of the then current programme to establish what should no longer be included in the programme;
- an extension of the programme to cover a 5 rather than 3 year period;
- the identification of areas for improvement in the management of the programme.

6.3. The capital programme has been reviewed, formally removing £101.4m from the capital programme, as detailed in the Capital Report (elsewhere on this agenda), to:

- reduce capital expenditure to focus on existing contractual commitments, fulfilling statutory services and public safety requirement in line with the s.114 Notice
- reduce reliance on borrowing from £40.1m to £4.9m for the General Fund and from £115m to £96.2m for the HRA;
- formally remove the capital projects on hold of £119m with the associated borrowing of £62.9m
- formally remove the capital projects not yet started and deemed to be not required of £3.3m wholly funded from borrowing

7. Capital Receipts

7.1. As part of the improvement and recovery plan there is a strategy to dispose of over £100m of Property Assets to provide capital receipts over a 5-year period to support debt reduction. This is under review and will be updated in subsequent reports.

7.2. The Asset Disposals Team was set up in February and March 2023 and continues the ongoing work of reviewing and appraising properties within the team, consulting the legal team, other service areas, and commercial agents. This includes both legal and property due diligence that is essential for effective disposals.

7.3. The current position is that:

- Disposals complete to date £7.2m;
- Disposals with legal / conveyancer £40.7m;
- Disposals planned to March 2024 £47.9m;

8. Revenue

8.1. The Council generates the majority of its income from government grant, retained business rates (NNDR) and council tax. In 2024/25 the Council can raise council tax up to 9.99% via three percentage increases:

- Standard council tax, up to 3% annually;
- Adult Social Care precept 1.99%;
- DLUHC special resolution increase of up to 5%

8.2. Provisionally, the council tax is to be raised by a rate of 7.99%, with the foregone 2% rise being compensated for through a combination of further savings and reduced growth of £1.7m. This lower council tax increase will reduce future years council tax income by c£1.78m necessitating further annual savings to reduce the Capitalisation Direction requirements.

8.3. Excluding Treasury and Capital activities, the Council continues to have extensive service and operational revenue pressures, which are forecast to extend beyond 2028/29. The central government Capitalisation Direction, which enables the council special borrowing powers, are only granted annually and the Council must demonstrate its transformation activities are moving towards setting a self-sufficient balanced budget.

8.4. The MTFS revenue budget brings together the anticipated full effect of the councils' core funding, operational service budgets, savings targets and the effect of ongoing debt costs for the council.

8.5. Decisions regarding funding and operational spend in 2024/25 have a significant effect on the future capitalisation directive funding requirements, which attracts interest costs and thereby the council's ability to achieve financial sustainability as soon as possible.

8.6. The key drivers in delivering a balanced budget are:

- the level of Council Tax and Business Rates (NNDR) agreed by Council;
- the Core Funding received from central government;
- the impact of pay inflation and pressures;
- historic pressures and growth in services;
- target savings;
- the expected impact of investment and property disposals,
- net effect of interest rates and level of borrowing;
- Minimum Revenue Provision;
- ongoing Capitalisation Direction requirements (borrowing);
- required levels of contingency and reserves.

8.7. The MTFS is built upon the drivers in paragraph 8.6, the key assumptions are summarised below and detailed in Appendix 2:

- the Council increases council tax by 7.99%, comprising of the 3% pre-referendum limit, Adult Social Care (ASC) ringfenced precept of 1.99% and DLUHC special resolution authority of 2.99% in 2024/25 and continue to increase council tax by 3% pre-referendum limit and ASC 1.99% thereafter;
- in 2024/25 Business Rates (NNDR) increase in line with inflation, plus an anticipated £2.5m via the Business Rates (NNDR) Pooling, s31 grant of £1m and an adjustment for the prior year collections, which are estimated at this time;
- in 2024/25, inflation of £8.7m is represented by up to 6.7% on qualifying non pay expenditure (subject to approval), a combined increase of c5.8% for pay inflation and increments; all forecast to both reduce to c2% in later years;
- there are specific service pressure resolutions totalling £5m, based on Q3 budget monitoring, plus service growth of £6m in 2024/25, offset by the halving of the intervention budget; thereafter the service growth is forecast to rise at c£6.2 - £7m pa;
- initial recurrent savings targets of £18.2m in 2024/25 and a further £18.2m in 2025/26, with ongoing years targeted to generate additional recurrent £13.6m pa each year through to 2028/29;
- additional saving of £1.7m in 2024/25 if the DLUHC approved council tax increase is 2.99% instead of the approved 5%;
- divestment of the investments and asset sales will significantly reduce the anticipated Capitalisation Direction by £522m, to £520m and reduce the General Fund Debt by £978m over the next 5 years;
- investment and asset disposals are anticipated to reduce the forecasted interest and MRP costs by £103.7m, from £156m to £52m, in 2024/25, ongoing costs are expected to be £50m pa due to MRP, Capitalisation Direction and outstanding debts (Appendix 3);
- the MTFS is modelled on PWLB interest rates reducing from 4.7% in 2024/25 to a low of 3.5% in 2028/29 and interest is forecast to reduce to £19m in 2024/25 and c£17m thereafter;

- the MRP charge is expected to be £33.1m in 2024/25, including £8.5m MRP on the Capitalisation Direction respectively. Thereafter MRP will stabilise at around £35m per annum, once disposals are realised;
- the Capitalisation Direction requirement is anticipated to reduce if disposals are achieved, and the Council continues to make significant annual savings as stated above via service delivery changes:
- the council should hold sufficient contingency to manage risks of the council activities and mitigate challenging demands such as savings targets. Reserves need to be adequate to manage unforeseen events and stabilise periodic pressures. The council's level of reserves should be a minimum of £11m.

8.8. The detail relating to 2024/25 budget is contained within the Revenue Budget 2024/25 Report, which is outlined in another part of the agenda.

8.9. The Councils funding and spending forecasts, together with Capital Directive requirements are summarised below. The Net Cost of Services continues to rise annually and there is strong reliance on savings to reduce the Capitalisation Direction support required

8.10. The Capitalisation Direction adjustment relates to backdated MRP and asset impairments, which impacts the 2023/24 Capitalisation Direction requirement via MRP and interest charges.

	2022/23	**2023/24**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Original budget	452	180	157	69	66	62	56	**1,042**
Revised	40	235	69	59	51	43	24	**520**
Change	(412)	55	(88)	(10)	(15)	(19)	(32)	**(522)**

Table 3 – Council funding, spending and Capital Direction requirement

	BASE BUDGET	FUTURE YEARS CHANGE TO BASE BUDGET			
	2024/25	**2025/26**	**2026/27**	**2027/28**	**2028/29**
	£000's	**£000's**	**£000's**	**£000's**	**£000's**
Total Core Funding	(154,613)	(663)	(7,583)	(7,960)	(8,354)
Total Service Cost before savings	187,628	9,600	11,992	12,443	12,912
Total Treasury costs	52,169	(694)	2,126	301	(9,399)
	85,184	**8,243**	**6,536**	**4,783**	**(4,841)**
Saving targets*	(16,615)	(18,200)	(13,650)	(13,650)	(13,650)
Total net (income) / costs	**68,569**	**(9,957)**	**(7,114)**	**(8,867)**	**(18,491)**
Use of capitalisation funding	0	68,569	58,611	51,497	42,630
Capitalisation Direction Requirement	**68,569**	**58,611**	**51,497**	**42,630**	**24,140**

*Original saving of £18.2m plus £1.7m Council Tax, less £3.3m included in Council Tax and Business Rates income

9. Treasury

9.1. The treasury element of the budget consists of the three entries:

- Interest Payable and Investment Income
- Minimum Revenue Provision (MRP) on the capital programme and investment assets
- Capitalisation Direction borrowing

9.2. The Council has developed a comprehensive treasury and capital financing model which has been used to calculate the budget requirement for 2024/25. This is based on the revised Treasury Management (TM) Strategy and Capital Strategy Report which is reported to Cabinet and Council in parallel with the 2024/25 budget setting reports (elsewhere on this agenda).

9.3. The interest payable is based on the forecast from Link, the Councils TM advisors, with a borrowing rate of 4.7% predicted for the financial year.

9.4. An underpinning principal of the local authority financial system is that all capital expenditure must be financed either from capital receipts, capital grants (or other contributions) or eventually from revenue income via an MRP charge. MRP is the charge to revenue made in respect of repaying the principal element of borrowing undertaken to finance projects in the capital programme.

9.5. The MRP policy is set out within the Treasury Management Strategy and the charge is part of the detailed treasury model that underpins 2024/25 budget setting.

9.6. In line with the Councils MRP policy, the Council makes provision for the write down of the debt that is funding capital investment assets. There has been a significant reduction in the projected charge reflecting planned disposal dates for significant capital investments coming forward from 2024/25 to 2028/29. Once these assets have been disposed of there is now no requirement to make further MRP charges.

9.7. There are three key indicators of the progress being made or anticipated in 2024/25 and beyond, these are summarised in paragraph 1.3.

9.8. To reach financial sustainability the Council must eliminate the Capitalisation Direction. Debt Costs should be reduced to manageable levels, below 10% of core funding, which at a rate of 3.5% would be £17.9m. The 3.5% is an estimation of the PWLB borrowing rate in 2028/29, this is highly subjective and likely to change, an increase in the PWLB rate would proportionately reduce the debt funding ultimate target value.

9.9. The General Fund debt, at the end of 2024/25 is estimated to be £356m, and £314m at the end of the 5-year MTFS period in 2028/29.

Table 4 – Movement on General Fund Debt

Fund	2022/23 £'m	2023/24 £'m	2024/25 £'m	2025/26 £'m	2026/27 £'m	2027/28 £'m	2028/29 £'m	Reduction £'m
General Fund Debt	1,293	434	356	349	318	310	314	978

9.10. The detailed composition of the Councils debt and interest calculations are contained within the Treasury Management Strategy Report. However, to put the £314m estimated General Fund debt figure into context, this was £1.293bn at the time of setting the 2023/24 base budget. This very significant reduction is as a result of the disposal of investment and fixed assets, and a reduction in both the current and planned Capital programme.

9.11. In 2024/25, the cost of servicing the Councils General Fund debt position will be £52.17m. This represents 33.74% of the Councils total net resources raised through Council Tax, retained business rates, and central government core grant funding. This should typically be between 5% to 10% and remains a key obstacle to returning to financial sustainability.

9.12. As shown in Appendix 3 the total expenditure budget for Debt Management costs has reduced from a budgeted £155.84m in 2023/24 and a forecast £203.9m to £52.17m in 2024/25. See section 10.

10. Capitalisation Direction Revenue Impact

10.1. Following legal advice there has been a late change in the technical calculation of the MRP, which has impacted the Capitalisation Direction calculation. It relates to the treatment of historic MRP charges, these are now required to be recognised in the current and future years. Work continues to refine these calculations.

10.2. The impact on the revenue budget of the Capitalisation Direction (CD) is twofold, MRP and the associated interest costs arising from the element of borrowing that is required to fund the operational budget deficit to the extent this is required, interest is charged at a premium of 1% above the standard PWLB 20 year rate.

10.3. The annual CD requirement is subject to yearly DLUHC approval and for 2024/25 was approved in autumn 2022 at £156.5m as part of the overall estimated CD requirement of £1,042m to 2028/29.

10.4. During the year the anticipated total Capitalisation Direction requirement to 2028/29 has been revised, significantly reducing the annual support from a 5 year total of £1,042m originally forecast to a revised estimate of £520m by 2028/29. The reduction is summarised in the table below.

MTFS Revised Capitalisation Direction Forecast	**£m**
Original CD requirement	1,042
CD restatement 2018/23	- 412
In year CD increase	55
Forecast CD reduction	- 165
Revised CD requirement	**520**

10.5. The reduction in the CD over the 5 year period compared with the previous 2023/24 MTFS reflects the following:

Capitalisation Direction Restatement to future years	
	£m
Asset Impairment	-275
Backdated MRP	-54
2022/23 MRP	-75
Other in year movements	-8
-	**-412**

- Misclassification of the impairment of investment assets as a revenue charge in the original CD. Because the majority of the investment assets were statutorily defined capital expenditure, the Council should already have been providing MRP on that expenditure. To then charge an impairment to the revenue account would be double counting. Correction for the impairment of investment asset reduces the overall CD by £275m;
- Changing the correction of the understatement of MRP from being a retrospective adjustment in years prior to 31 March 2023 to a forward look change from 1 April 2023 (i.e. in the current financial year). This follows legal advice that, notwithstanding that the MRP policies which the Council had approved in previous years did not follow the statutory MRP Guidance, the MRP policies in those years were approved in line with the Council's decision-making processes and thus lawfully set. This reduces the CD in 2022/23 by £54m for backlog MRP.
- There is an increase in the MRP charge in 2023/24 of £76m to £154.8m, which increases the total overall CD for 2023/24 by £55m to £235m from £180m;
- A rigorous review of the capital programme 2023/24 to 2028/29, reported elsewhere in this agenda, which has reduced the reliance on borrowing for the capital programme by £101m, which reduces the MRP

- Consistently reducing annual treasury costs down to c£35m in 2024/25 and c£30m thereafter.

10.6. It should be noted that the unprecedented scale of the financial position created by the Council's decision to borrow to invest and establish remedies for this, mean that dealing with this has been subject to advice from a number of parties – CIPFA, DLUHC, External Audit and at their request KC's advice. Notwithstanding the inadequacies of the information reported to Members in setting previous years' MRP policies, those policies were lawfully made. Hence any changes should only be made prospectively from 1 April 2023.

10.7. The forward look estimate of the Capitalisation Direction requirement continues to be subject to ongoing review and the balances included in the MTFS reported below reflect the latest modelled position

Table 5 – Capitalisation Direction Forecast

	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	Total
	£m	£m	£m	£m	£m	£m	£m	£m
Original budget	452	180	157	69	66	62	56	**1,042**
Revised	40	235	69	59	51	43	24	**520**
Change	(412)	55	(88)	(10)	(15)	(19)	(32)	**(522)**

11. Government Directions and Related Reports

11.1. This has been reported on elsewhere to Cabinet, for completeness the financial element is included also below:

Priorities	Workstreams	Aims	Objectives
Improving Financial Sustainability	Divestment of the Council's investments	We will have significantly reduced the debt of the Council and reduced the budget financing debt charges to secure a more stable financial position in the longer term to mitigate future risks.	Dispose of investments
	Improving our stability through budgetary savings and maximisation of income	We will have implemented a range of actions to demonstrate significant savings, reductions in the capital programme, generation of capital receipts - all of which will lead to the significant reduction in general fund borrowing – as well as maximisation of income to pay down a proportion of our debt and ensure that service and programme spending delivers the highest level of service and outcomes within the constrained resources available. Spending controls as a result of the Section 114 notice have also supported in delivering this objective.	Through implementing a savings programme, alongside a programme to maximise income over each of the next five years and beyond, the Council's budget moves towards achieving a balanced position.
			Detailed plan to generate capital receipts
			Develop a Capital Programme which leads to General Fund borrowing which is significantly smaller and aligned to the Corporate Plan.

Priorities	Workstreams	Aims	Objectives
	Improving our financial management capability and practice	We will have a fit for purpose finance function that demonstrates exemplary leadership and management, implements robust financial controls, and champions effective scrutiny and reporting to enable clear accountability, risk management and compliance with statutory requirements and accounting standards. That there is strong and appropriate financial capability for leaders, budget holders and members enabling them to fulfil their own fiduciary duties and engage meaningfully in scrutiny and challenge.	Demonstrate exemplary corporate financial leadership
			Redesign and restructure the Council's financial service
			Corporate Financial Capability

12. Council Operating Model

12.1. The council is committed to driving significant culture change across the organisation, it recognises and acknowledges the challenge of rebuilding the trust and confidence of people inside and external to the organisation. The scale of change starts with its new purpose (Enabling Council), vision and strategic aims and a new operating model being designed, developed and implemented.

12.2. To deliver this significant change, there is a programme of a minimum of three years from 2022 to 2025, impacting across all aspects of people management, leadership, work practices, customer contact and service delivery as well as individual behaviour and cultural change.

12.3. The leadership of the council is committed to agreeing jointly and to adopting new values and behaviours to change the culture and practices of the organisation. This will support the Council's workforce to continue to deliver for its residents, businesses and other stakeholders and allow the Council to maximise the huge opportunities the borough and council has within its grasp.

13. Financial Management

13.1. This is dealt with in the Section 25 Report earlier in this agenda.

14. Reasons for Recommendation

14.1. The recommendation is made in order that the Council is clear about its MTFS, the basis on which it is constructed and the targets it is working towards,

15. Consultation (including Overview and Scrutiny, if applicable)

15.1. Consultation has taken place with the Commissioners and the report has been considered by Scrutiny.

16. Impact on corporate policies, priorities, performance and community impact

16.1. The delivery of the MTFS will underpin all of the work of the Council and it policies, priorities and performance

17. Implications

17.1. Financial

Implications verified by: **Laura Roberts**

Finance Consultant

These are set out in the main body of this report.

17.2. Legal

Implications verified by: **Jayne Middleton-Albooye**

Interim Head of Legal Services

The approval of the MTFS is part of the overall budget approval process. The setting of the budget is a function reserved to Full Council. A local authority is required under the Local Government Finance Act 1992 to produce a 'balanced budget'. Furthermore, the Council is subject to the Best Value duty under the Local Government Act 1999 to secure continuous improvement in an efficient, economic and effective way.

Section 25(1)(a) and (b) of the Local Government Act 2003 requires its Chief Finance Officer (Section 151 Officer) to report amongst other things, on the robustness of the estimates made for the purpose of calculating Council Tax, and on the adequacy of reserves.

Separate specific legal advice has been given in relation to any agreed savings options, and is also set out in separate reports to Council such as the Revenue Budget Report and the Council Tax Base report.

In addition, the Council when exercising its functions must have due regard to its equalities duties under section 149 of the Equality Act 2010.This can be achieved by considering the equalities and diversity implications at all stages of the budget setting process to ensure that budget proposals do not discriminate against any of the protected equality groups.

17.3. Diversity and Equality

Implications verified by: **Rebecca Lee**

Community Development and Equalities Manager

There are no specific diversity and equalities implications as part of this report.

Community and Equality Impact Assessments (CEIAs) have been completed for specific budget proposals.

17.4. Other implications (where significant) – i.e. Staff, Health Inequalities, Sustainability, Crime and Disorder, or Impact on Looked After Children

None

18. Background papers used in preparing the report

(including their location on the Council's website or identification whether any are exempt or protected by copyright):

19. Appendices to the report

- Appendix 1 – Recommendations form Secretary of State
- Appendix 2 – MTFS Assumptions
- Appendix 3 – Total Resources and Treasury Management Costs

Report Author:

Steven Mair

Interim Chief Finance Officer / s151

Finance Department