

NORTHUMBRIA POLICE AUTHORITY

MEDIUM TERM FINANCIAL STRATEGY 2009/10 – 2011/12



Northumbria Police Authority

Medium Term Financial Strategy 2009/10 – 2011/12

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1. Purpose of the Medium Term Financial Strategy

- 1.1 The current Medium Term Financial Strategy (MTFS) covering the period 2008/09 to 2010/11 was approved by the Police Authority on 21 November 2007. An updated Strategy to reflect the Chief Constables proposal to increase operational capacity to ensure delivery of the 2020 Vision was approved by the Police Authority on 23 January 2008. Although the strategy covers a period of 3 years, it is reviewed annually to reflect the dynamic nature of both policing and changes in funding.
- 1.2 The MTFS is a key part of the Authority's Integrated Corporate Planning Process which links operational planning with financial and resource planning, to ensure that all resources are directed toward policy priorities. The Strategy describes the financial direction of the Authority and outlines the financial pressures over a 3 year period. It is also an indication of the likely direction of financial planning over the next year.
- 1.3 The MTFS provides options for delivering a sustainable budget and capital programme over the medium term and sets out how the Authority can provide the Chief Constable with the resources to deliver the priorities in the local policing plan and the 2020 Vision.
- 1.4 Following consideration of the MTFS, a financial strategy is agreed and specific proposals developed for consultation with stakeholders and reviewed in January before the Authority agrees its revenue budget and capital programme in February of each year.

2. Benefits of the Strategy

- 2.1 The MTFS assists in:
 - Aligning financial resources to the Authority's spending priorities
 - Responding to the Chief Constable's resource requirements
 - Meeting strategic priorities and the requirements of the policing plan
 - Supporting the delivery of the 2020 Vision
 - Improving financial planning and the financial management of the Authority's resources, both revenue and capital
 - Maximising the use of resources available to the Authority, both internal and external
 - Ensuring that the Authority provides Value for Money and continues to achieve efficiency gains
 - Allowing the development of longer term budgets and strategic thinking
 - Reviewing the Authority's policy on the use of reserves, ensuring the position continues to be positive and there are sufficient resources over the medium term
 - Responding to external pressures, including changes to the police funding formula
 - Developing a sustainable budget over the medium term

3. Principles of the Strategy

3.1 The key principles underlying the Authority's MTFs 2009/10 to 2011/12 are:

- (i) The Authority's resources will be directed to achieving the Authority's priorities as expressed in the Local Policing Plan;
- (ii) Overall Authority expenditure should be contained within original estimates each year;
- (iii) The Authority will maintain its general reserve at a minimum of 5% of its gross revenue budget to cover any major unforeseen expenditure and will consider on a regular basis the opportunity cost of maintaining reserves balanced against the benefits derived from income earned and protecting against risks;
- (iv) The Authority will aim to balance its revenue budget over the period of the MTFs without reliance on the use of general reserves;
- (v) The Authority will maintain earmarked reserves for specific purposes, which are consistent with achieving its priorities. The use of earmarked reserves will be in line with the principles set out in the MTFs and reviewed annually;
- (vi) The Authority will continue to improve its approach to efficiency and value for money;
- (vii) The Authority recognises the impact of increases in precept levels in an area of relatively low income and low wealth (as measured by property values) and will balance the need for increases in precept against the delivery of the Authority's priorities;
- (viii) The Authority will consider the use of prudential borrowing to support the capital programme as part of its annual Treasury Strategy and will ensure that the revenue costs are affordable;
- (ix) The Authority will continue to contribute to reviews of police funding, both in its own right and as a member of lobbying groups such as the Association of Police Authorities;
- (x) The Treasurer and Chief Constable will prepare a rolling programme of 3 year budget forecasts;
- (xi) Opportunities for securing external funding to support the Authority's priorities will be sought. The implications of the cessation or withdrawal of funding will also continue to be reviewed so that options can be considered on the future of the funded schemes; and
- (xii) Opportunities for working in collaboration and partnership will be identified and developed where this will support the Authority's corporate priorities and improve service efficiency and delivery.

4. Reviewing the Strategy

4.1 The review of the Authority's MTFs for 2009/10 to 2011/12 has been carried out under the following headings:

- The financial environment in which the Authority operates;
- The Authority's financial position;

- The future budget pressures which the Authority is likely to face over the period of the strategy;
- The Authority's Capital Programme;
- Reserves Policy;
- Police Funding Formula; and
- The Government's Efficiency Review.

5. Financial Environment

- 5.1 Over the past few years precept increases nationally have been constrained by the Government's threat of capping. The proportion of funding from formula grant has reduced, and the proportion from council tax and Specific Home Office Grants has increased. Income from precepts represents only 12% of the Authority's spending.
- 5.2 The Comprehensive Spending Review (CSR07) was announced in October 2007 setting out the Government's overall funding plans for 2008-2011. Consistent with this, the Minister of State for Local Government announced, on 26 November 2008, details of the provisional 2009/10 and 2010/11 Local Government Finance Settlement. The provisional settlements for Northumbria are unchanged with an increase of 2.5% in both years, the minimum possible.
- 5.3 The downturn in the economy and the injection of public funding into the banking sector is likely to have an impact on the level of public spending in the future. The Chancellor's pre budget report on 24 November 2008 announced some measures to stimulate the economy such as the immediate VAT reduction. This and other measures will be balanced by a proposed increase in the National Insurance rate of £0.5% in April 2011 and an extra £5 billion public sector efficiency savings in 2011/12. Local authorities, including police authorities will need to contribute to this additional requirement given that overall public spending will rise by only 1.2% from 2011 onwards.
- 5.4 The Authority have a £3.5m deposit in Heritable Bank, a subsidiary of an Icelandic bank, which is currently in administration. Positive progress is being made to recover the deposit and it is not expected that there will be any impact on the Authority's medium term financial position. This is supported by an announcement by the Government that regulations will be introduced to ensure any losses do not impact on precepts until 2010/11 at the earliest.
- 5.5 Options to mitigate the impact of the current economic position including the repayment of debt are being considered and will be presented for consideration as part of the revised Treasury Management Strategy in the New Year.

6. Authority's Current Financial Position

- 6.1 The net revenue budget for 2007/08 was £270.145m, comprising a total police expenditure requirement of £278.145m offset by transfers

from reserves of £8.00m. Effective budget monitoring and delivery of efficiencies during the year ensured that expenditure was contained within original estimates.

- 6.2 Sound financial management has allowed the Authority to consistently provide for high priority growth identified by the Chief Constable. It has also been possible to prudently add to the level of reserves in recent years, particularly those available for capital investment. All of this has been achieved with the lowest precept level in the country.
- 6.3 The Authority's net revenue budget for 2008/09 provides for total police expenditure of £277.822m after the use of reserves. The second quarterly revenue monitoring report which was presented to the Resource Management Committee in October showed a notional underspend of £2.135m as at 30 September 2008. This position, six months into the financial year, satisfies one of the key principles of the MTFS of containing spending within original estimates.
- 6.4 The second quarter capital monitoring report to October's Resource Management Committee outlined a reviewed capital estimate of £25.049m as at 30 September 2008, compared to the original estimate of £28.237m. This is largely due to site preparation work for the site for North Tyneside Area Command. Given the high number of major building schemes in the programme, where the timing of expenditure is uncertain this reviewed estimate is subject to fluctuation and it will therefore be closely monitored for the rest of the year, supported by a quarterly update of the Estates Strategy.

7. Medium Term Budget Pressures

- 7.1 An initial assessment suggests that pay and price increases of £7.5m and commitments of £4.8m will need to be met in 2009/10. This includes the full year effect of 2008/09 growth, pay increases of 2.65% and price increases estimated at 2.5%. The impact of the use of reserves and revenue costs from implementation of the Estates Strategy will add an extra £2m to growth. For 2010/11 and 2011/12 the base budget is also expected to increase for pay and prices by £7.7m and £7.9m respectively. In addition, the initial prioritised revenue proposal identified by the Chief Constable during the revision of the strategy is in relation to the requirements for connection and utilisation of the IMPACT Police National Database (PND). This service will be effective from 31 December 2010 and is intended as the National Police Intelligence System.
- 7.2 The financial impact of these commitments and proposals are shown in Section 11 of this strategy.

8. Capital and Prudential Borrowing

Impact of Capital Programme

- 8.1 The following table outlines the estimated effect that prioritised capital proposals could have on the overall capital programme over the next three years. These proposals have been identified during the revision of the MTFS and include budget revisions and slippage carried forward to 2009/10:

	2009/10 £m	2010/11 £m	2011/12 £m	TOTAL £m
High Priority Proposals				
Major Building Schemes	25.336	30.510	41.518	97.364
Minor Building Schemes	1.515	1.192	0.450	3.157
IS & T	6.780	6.330	1.427	14.537
Vehicles / Equipment	4.179	4.792	3.872	12.843
	37.810	42.824	47.267	127.901

- 8.2 The major component of the estimated capital programme over the next 3 years is the continuing delivery of the Estates Strategy. The cost of the Strategy in the years 2009/10 to 2011/12 is estimated at £97m. Prioritisation and phasing of these major building schemes was considered as part of the review of the Estates Strategy presented to the Resource Management Committee in December 2008.
- 8.3 The capital budget forecast also takes account of the Corporate Planning process and the need to routinely replace assets which have come to the end of their useful working life.
- 8.4 The proposal for IS & T capital expenditure provides for the ongoing 'refresh' of the existing technology and supporting equipment in line with the principles of the IS & T Strategy presented to the Resource Management Committee in November 2008. Provision is also included for the continued rollout of the Voice and Data Storage Area Network and the planned technology and application server refresh.
- 8.5 The proposed vehicle budget provides for the continued replacement of operational vehicles in line with the current vehicle replacement policy.

Impact of Prudential Borrowing on the Budget Position

- 8.6 As well as the use of capital resources which could be received in 2009/10 and future years such as the generation of capital receipts, the Authority will need to apply earmarked capital reserves and / or prudential borrowing to implement the capital programme.

8.7 The estimated capital budget requirement can be summarised as follows:

	£m
2009/10	37.810
2010/11	42.824
2011/12	47.267

8.8 It has been confirmed that the level of central government capital grant and supported borrowing contributions to capital are to remain at 2008/09 levels. Previously the strategy has been to use capital reserves to implement the capital programme, supported where necessary by prudential borrowing. Due to a change in rules for calculating the Minimum Revenue Provision (MRP) charge, and the current market conditions, it is a more attractive option to use the Capital Development Reserve to finance the revenue costs of prudential borrowing rather than applying to outright capital purchases, particularly for the Estates Strategy. If account is taken of these factors, and assuming a minimum level of capital receipts over this MTF5, then the need for prudential borrowing can be summarised as follows:

	£m
2009/10	33.238
2010/11	37.252
2011/12	42.695

8.9 The borrowing and reducing capital reserves have a revenue impact by way of the interest payments on the borrowing and the interest lost on the investment of reserves. In addition to the revenue impact of interest, undertaking prudential borrowing will also impact on the Minimum Revenue Provision (MRP), the amount charged to revenue for the provision of the repayment of external loans. The estimated revenue impact is as follows:

	Interest lost on reserves £m	Interest cost of borrowing £m	Total interest cost £m	MRP on additional borrowing £m	Total Revenue impact £m
2009/10	0.101	1.496	1.597	0	1.597
2010/11	0.278	3.217	3.495	2.716	6.211
2011/12	0.470	5.138	5.608	5.578	11.186

8.10 The most cost effective method of financing the proposed capital programme will need to be considered alongside the annual review of the Treasury Strategy in the New year which will take into account interest rate forecasts and rapidly changing market conditions.

9. Reserves

Reserves Policy

Sections 32 and 43 of the Local Government Finance Act 1992 require billing and precepting authorities in England and Wales to have regard to the level of reserves needed for meeting estimated future expenditure when preparing budgets.

In establishing reserves, the Authority must comply with the Code of Practice on Local Authority Accounting in the United Kingdom (the SORP).

The Authority reviews its reserves policy at least twice a year when preparing its annual budget and reviewing the MTFs. By doing this, the visibility of reserves are increased and consideration of their use is placed at the forefront of the decision making process. Revenue reserves are cash backed balances, held on the balance sheet until they are spent or released for other purposes. As such, they can only be spent once, and are not part of the base budget.

The Authority's balance sheet reserves are held for three main purposes:

- A contingency to cushion the impact of unexpected events or emergencies for example, a change in protection arrangements in the police funding formula – this forms part of the general reserve;
- A working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this too forms part of the general reserve; and
- A means of building up funds to meet known or predicted liabilities or to smooth expenditure requirements – known as earmarked reserves. The Capital Development Reserve is an example of this sort of reserve.

9.5 There is no statutory guidance on the right level of reserves. CIPFA guidance issued in June 2003 confirms that authorities on the advice of their Treasurers should make their own judgements on such matters, taking into account relevant local circumstances and an assessment of risk.

9.6 The Authority's policy on reserves as reflected in the MTFs principles is as follows:

- The Authority will maintain its general reserve at a minimum of 5% of its gross revenue budget to cover any major unforeseen expenditure.
- The Authority will aim to balance its revenue budget over the period of the MTFs without reliance on the use of general reserves.
- The Authority will maintain earmarked reserves for specific purposes, which are consistent with achieving its priorities. The

use of earmarked reserves will be in line with the principles set out in the MTFs and reviewed annually.

- 9.7 The Authority must retain adequate reserves so that unexpected demand led pressures on its budgets can be met without adverse impact on the achievement of the Authority's key priorities and council tax payers. The Authority's policy for reserves and balances should be based on a thorough understanding of its needs and risks. Part of this process is to give clearer explanation of the existing and proposed use of reserves and this is addressed in the paragraphs below.
- 9.8 Revenue reserves fall into two categories, general and earmarked. Reserves will be dealt with in more detail in the following paragraphs, but the position as at April 2008 can be summarised as follows:

	£m
General reserve	46.208
Earmarked reserves	<u>17.737</u>
	63.945

- 9.9 CIPFA defines revenue reserves as "resulting from events that have allowed monies to be set aside, surpluses or decisions causing anticipated expenditure to have been postponed or cancelled."

General Reserve

- 9.10 The Authority's general and earmarked reserves have always been retained at a prudent level and are subject to a regular review. The general reserve is available to support future revenue budgets and capital programmes, as well as protecting the Authority in the event of a major incident. The MTFs allows the Authority to consider the prudent use of reserves in the context of the future spending pressures, risks and changes to the funding formula without having a detrimental effect on policing in Northumbria.
- 9.11 The general reserve of £46.208m as at 1 April 2008 is 14.1% of gross expenditure and 16.1% of net expenditure. Guidance does not dictate a reasonable level of general reserve because it needs to be linked to other factors such as the risks inherent in the budget, the robustness of budget monitoring, past experience of outturn spending and the extent of earmarked reserves. All of these factors which are positive suggest that the general reserve, which is designed to act as a contingency and smooth out variations in spending, could be reduced to a minimum level of £16.5m over the medium term. This would equate to 5% of gross expenditure. This allows the Authority to use the general reserve for the next 3 years as short term funding to continue to allow the outcomes of the Chief Constable's growth proposals to deliver the 2020 Vision to be realised in advance of planned efficiency savings.

Earmarked Reserves

- 9.12 Earmarked reserves are set up to provide for specific liabilities. The major liabilities covered by these reserves are pensions and insurance.
- 9.13 A number of appropriate purposes for the creation of earmarked reserves have already been identified in previous years. The current reserves and their rationale are set out as follows:

Insurance Reserve

The insurance reserve is maintained for potential liabilities and costs, which fall onto the Authority where no external insurance cover is arranged by or available to the Authority. Potential liabilities include storm damage, business interruption and claims that would fall within the Authority's policy excess limit. In line with the requirements of the SORP, the Authority operates an Internal Insurance Account, where internal premiums are charged and any surpluses generated are credited to the reserve. Given the difficulties encountered in previous years of securing external cover, this reserve protects the Authority from changes in the insurance market. In line with good practice this reserve is reviewed annually with the outcome reflected in the following year's budget. Following a review as part of last year's MTFS, the insurance reserve was reduced to £6m, and the balance applied to support revenue spending. Given the nature of this reserve it is not appropriate to show any movement over the life of the MTFS..

Devolved Budget Reserve

The Authority has approved a scheme of financial devolution to ensure that responsibility and accountability for resources rests with those managers who are responsible for service delivery. To make the scheme work and give devolved budget holders the necessary freedom to manage their resources, they are allowed to carry forward underspends. This amount represents the cumulative net underspend of the budget devolved to specific departments and area commands which is carried forward into the following financial year to cover future events. A limit on the size of the carry forward was applied last year, equivalent to 4% of the devolved budget. This equates to an amount of £2.26m, and any balance exceeding this will be transferred to the general reserve, and applied to support agreed schemes in 2009/10.

Air Support Unit General Reserve

This represents the cumulative net unspent element of the Air Support Unit (pertinent to Northumbria) that is carried forward into the next financial year. The reserve is maintained to allow for future unexpected events, Northumbria's current balance held is £0.571m.

Police Officers Commutation Reserve

This reserve was originally a provision for the cost of lump sum payments in respect of those officers eligible to retire as at the balance sheet date. Following the introduction of accounting requirements for pensions this has been reclassified as a reserve. The principal reasons for maintaining the reserve are:

- The Authority's responsibility for the costs of ill health retirement and the need for a reserve to smooth the costs year on year.
- Given the uncertainty over the impact of the new police pension arrangements and the need to cover ill health retirements, it was agreed by the Authority following the Revenue and Capital Budget Report 2006/07 presented 15 February 2006 that this reserve be retained in the medium term, facilitating contributions to revenue of £2.5m a year to allow time for the impact of the new pension scheme to be reviewed. This position was reviewed prior to consideration of precept levels in February 2007, when the Authority agreed to increase the contributions to revenue spending to £3m per annum for the next three years.

Airwave Reserve

This reserve is maintained to allow for the future costs associated with the national radio communications system. The balance of this reserve is £1m which will be used in 2010/11 to finance the replacement of the integrated command and control system.

Capital Reserves

- 9.14 The Authority retains capital reserves which comprise resources which can be applied for capital purposes i.e. to finance capital expenditure or to repay debt, and which are currently earmarked to support the Authority's Estates Strategy over the medium term. Capital Grants Unapplied and Capital Receipts Unapplied can only be used for capital purposes. In seeking to optimise the use of its estate, the Authority should be identifying opportunities to generate further capital receipts which would be added to the capital reserves and increase the Authority's capacity for capital investment. Given the uncertainty around the timing and scale of capital receipts, they have not been factored into the current projections. The capital reserves and their rationale are as follows:

Capital Grants Unapplied

This represents capital grants currently held by the Authority in order to finance future capital expenditure.

Capital Receipts Unapplied

This represents capital receipts currently held by the Authority in order to finance future capital expenditure.

Air Support Unit Capital Reserve

This represents the Authority's share of the Air Support Unit's capital reserve.

Capital Development Reserve

This reserve is to assist in developing and improving the capital assets of the Authority, particularly the Estates Strategy Development Programme. Consideration could be given to making use of this reserve to fund the revenue implications of prudential borrowing taken to support the delivery of the capital programme rather than applying to outright capital purchases. This would enable the Authority to take advantage and lock into current lower interest rates without impacting on the precept in the medium term. It is anticipated that following the completion of the major projects in the Estates Strategy, capital receipts will be received in respect of the former sites, which can be used to either repay debt or replenish this reserve.

Budgeted Reserves Position for 2008/09 and future years

- 9.15 A full analysis of the Authority's revenue and capital reserves and their planned use taking account of the proposals outlined in this report is as follows:

Analysis of proposed reserves 2008 to 2012

	At 31 March 2008 £000	At 31 March 2009 £000	At 31 March 2010 £000	At 31 March 2011 £000	At 31 March 2012 £000
NPA Reserves					
Revenue Reserves					
Earmarked Reserves					
Insurance Reserve	6,000	6,000	6,000	6,000	6,000
Devolved Budget Reserve	1,967	2,260	2,260	2,260	2,260
Air Support Unit General Reserve	571	571	571	571	571
Police Officers Commutation Reserve	8,199	5,199	2,199	0	0
Airwave Reserve	1,000	1,000	1,000	0	0
Total Earmarked Reserves	17,737	15,030	12,030	8,831	8,831
General Reserve	46,208	41,267	33,057	24,847	16,625
Total Revenue Reserves	63,945	56,297	45,087	33,678	25,456
Capital Reserves					
Capital Grants Unapplied	3,417	0	0	0	0
Capital Receipts Unapplied	8,720	0	0	0	0
Air Support Unit Capital Reserve	20	0	0	0	0
Capital Development Reserve	31,076	30,701	29,205	23,272	12,556
Total Capital Reserves	43,233	30,701	29,205	23,272	12,556

- 9.16 The above table is based on using the capital development reserve to fund prudential borrowing rather than for direct funding. This means that the reserve will remain at a higher level for a longer period compared to applying it directly to support the Capital Programme. It does, however, mean that it will be fully earmarked and planning will need to take place to ensure a sustainable position in the longer term. The changing economic situation means that alternative options can be considered that may be more favourable prior to the budget report in February.
- 9.17 The level of reserves carries an opportunity cost in that the funds held in reserve could be used for other purposes. This course of action has to be balanced against the benefits derived from income earned on reserves which is used to support the delivery of services and the need to make prudent provision for dealing with future risks and commitments.
- 9.18 The overall position of revenue and capital reserves will be further reviewed before the Authority agrees its annual revenue budget and capital programme in February 2009.
- 9.19 The Authority has previously agreed to draw £6.783m from the general reserve and £3m from earmarked reserves in 2008/09 to support revenue spending which is set to continue in 2009/10 and 2010/11. Following the inclusion of the projected £2.135m revenue underspend in 2008/09, it is proposed that £8.21m per annum is to be drawn from the General Reserve beyond 2009/10 to continue to support the revenue budget and the agreed strategy of reducing the General Reserve in the medium term to a minimum level of 5% of gross expenditure. The following table sets out the budgeted position for revenue reserves over the next 5 years:

NPA Revenue Reserves	Budget 2008/09 £000	Budget 2009/10 £000	Budget 2010/11 £000	Budget 2011/12 £000	Budget 2012/13 £000
Opening balances	63,945	56,297	45,087	33,678	25,456
Transfers to / (from):					
Earmarked reserve	(3,000)	(3,000)	(3,199)	0	0
Devolved reserve	293	0	0	0	0
General reserve	(4,941)	(8,210)	(8,210)	(8,222)	0
Closing Balance	56,297	45,087	33,678	25,456	25,456

- 9.20 In addition the Authority also has Capital Reserves. One of the options highlighted in the MTFS is the use of these capital reserves over the next 3 years. The following table sets out the position for capital reserves based on the capital proposals outlined in Para 8.1 over the next 5 years, assuming the use of the Capital Development Reserve to finance the revenue implications of prudential borrowing, with further options being modelled as part of the Annual Treasury Strategy:

NPA Capital Reserves	Budget 2008/09	Budget 2009/10	Budget 2010/11	Budget 2011/12	Budget 2012/13
	£000	£000	£000	£000	£000
Opening Balance	43,233	30,701	29,205	23,272	12,556
Receipts in year	4,572	4,572	4,572	4,572	4,572
(Payments in year)	(17,104)	(6,068)	(10,505)	(15,288)	(15,288)
Closing Balance	30,701	29,205	23,272	12,556	1,840

10. Funding

10.1 The Minister of State for Policing, Crime and Security announced details of the provisional Local Government Finance settlement for the financial years 2009/10 – 2010/11 on 26 November. There were no changes to the overall police formula grant allocations for Northumbria to the provisional figures set out in January 2008, with Northumbria provisionally receiving £249.9m, an increase of 2.5%. Northumbria's increase in grant funding is what is referred to as at the floor and without the application of floor damping, would have received £34.181m less grant in 2009/10, rising to £36.252m in 2010/11.

10.2 Provisionally the 2.5% increase for Northumbria continues for the two years and it would therefore be prudent to continue this trend when calculating the estimated grant funding for 2011/12. This would result in the following:

	2009/10	2010/11	2011/12
	£000	£000	£000
Home Office Grant	111,554	114,343	117,202
Revenue Support Grant	16,909	17,332	17,765
NNDR	121,472	124,509	127,622
Total Grant Funding	249,935	256,184	262,589

10.3 In relation to precept increases Ministers have said that "they will not hesitate to use capping powers to deal with excessive council tax increases in 2009/10, including requiring authorities to rebill if necessary".

10.4 The current reserves strategy is to draw £6.783m from the general reserve and £3m from earmarked reserves in 2008/09 to support revenue spending which is set to continue in 2009/10 and 2010/11. This position will be reviewed prior to the consideration of the revenue budget and capital programme in February 2009. Following the inclusion of the projected £2.135m revenue underspend in 2008/09, it is proposed that £8.21m per annum be drawn from the General Reserve beyond 2009/10 to continue to support the revenue budget

and the agreed strategy of reducing the General Reserve in the medium term to a minimum level of 5% of gross expenditure.

- 10.5 It is also proposed in the review of this MTFS to use prudential borrowing to finance the capital programme, funded by contributions from the Capital Development Reserve in the medium term. Contributions would be £1.496m in 2009/10, £5.933m in 2010/11 and £10.716m in 2011/12.

11. Indicative Budget Forecasts 2009/10 to 2011/12

- 11.1 An initial assessment suggests that pay and price increases of £7.481m and commitments of £4.807m will need to be met in 2009/10 which includes the full year effect of 2008/09 growth. This rises to £7.716m and £7.885m in 2010/11 and 2011/12 respectively. In addition, initial prioritised revenue proposals have been identified by the Chief Constable during the revision of the strategy. All the budget pressures outlined earlier in this document are summarised below, showing an overall position before consideration of the means of closing the projected funding gap:

11.2

	2009/10 £m	2010/11 £m	2011/12 £m
Base budget (before reserves)	287.271	300.294	311.093
Pay and price increases	7.481	7.716	7.885
	294.752	308.010	318.978
Budget Pressures			
Committed growth	4.807	1.055	0.670
Additional growth	0.169	0	0
Removal of non-recurring growth	0	(0.101)	0
Revenue impact of Capital strategy	1.597	4.614	4.975
Revenue impact of use of Revenue Reserves	0.369	0.315	0.249
	6.942	5.883	5.894
Planned efficiencies	(1.400)	(2.800)	(4.129)
Total Budget	300.294	311.093	320.743
Projected total grant income	249.935	256.184	262.589
Precept income (current levels)	33.775	33.775	33.775
Total Income	283.710	289.959	296.364
Agreed use of reserves	12.706	16.342	18.938
Funding Gap	3.878	4.792	5.441

12. Funding Gap and Financial Strategy

12.1 The indicative budget forecasts outlined in Para 11.1 show a potential funding gap of £3.878m in 2009/10, increasing to £5.441m in 2011/12. This increasing gap is partly a reflection of the fact that an increase in precept or any additional use of reserves above the strategy previously agreed have not been factored into the assumptions. Both of these assumptions will need to be revisited to close the gap along with other options. Further refinement of the proposals will take place over the next two months to enable the Authority to consider the overall picture. Options open to the Authority to close the projected gap are as follows:

- Additional efficiencies
- Precept increases
- Reassessment of priorities
- Further use of reserves
- External funding / increases in income
- Review of existing borrowing

Additional Efficiencies

12.2 Opportunities for additional efficiencies are constantly being sought in order to continuously improve the Value for Money of the policing service provided in Northumbria. Permanent efficiencies delivered in one year will assist in reducing the gap for future years. The Authority and Force's approach to Value for Money is recognised in the Audit Commission's assessment of Use of Resources with the highest score possible.

Council Tax Precept

12.3 Each 1% increase in the precept generates £0.338m before taking into account changes in tax bases. Given that ministers have made it clear that council tax increases are expected to be under 5%, the illustration below only models council tax increases up to 5%. An increase of 5% (Band D increase from £78.27 a year to £82.18 a year) would generate £1.689m in extra revenue in 2009/10. An increase in one year would also reduce the gap in future periods. The cumulative additional income generated for a range of precept increases can be illustrated as follows:

	2009/10		2010/11		2011/12	
	Band D	Additional Income	Band D	Additional Income	Band D	Additional Income
	£	£m	£	£m	£	£m
0%	78.27	0	78.27	0	78.27	0
1%	79.05	0.338	79.85	0.679	80.64	1.023
2%	79.84	0.676	81.43	1.365	83.06	2.067
3%	80.62	1.013	83.04	2.057	85.53	3.132
4%	81.40	1.351	84.66	2.756	88.05	4.217
5%	82.19	1.689	86.29	3.462	90.61	5.324

Use of Reserves

- 12.4 The reserves strategy outlined in this document will result in earmarked reserves of £8.831m at the end of 2011/12, and a General Reserve of £16.625m. A reassessment of these reserves could enable an increase in the amount of revenue reserves used to support the revenue budget in the medium term. However, the use of reserves to support the budget is not sustainable in the longer term, and this reliance should be reduced as the benefits of efficiency initiatives put in place by the Force start to be realised.

Reassessment of Priorities

- 12.5 A further option for closing the funding gap is to reassess the current base budget including the funding of the capital programme and the level of priority growth proposed by the Chief Constable. Work on this will take place in the next 2 months to inform the revenue budget debate but, given that all of the growth shown in Section 11 is either committed or assessed as priority, there is limited scope to reduce this further.

External Funding / Increases in Income

- 12.6 The Authority and Force has been successful in securing and delivering outcomes from external funding in previous years. Specific and general funding will continue to be sought in line with the principles set out in this strategy.

Review of Existing Borrowing

- 12.7 The changing economic environment and falling rates of interest offers opportunities to review existing levels of borrowing. Historic borrowing taken out when interest rates were significantly higher can potentially be settled, either by utilisation of reserves or taking out equivalent borrowing at more favourable rates, reducing the revenue costs of servicing the debt.

13. Risk Assessment

- 13.1 The MTFs contains the most up to date information at the time of drafting but the Authority's financial position is dynamic. A comprehensive financial risk assessment is undertaken for the Revenue and Capital Budget setting process to ensure all risks and uncertainties affecting the Authority's financial position are identified. The Authority faces a number of financial uncertainties that could affect its position over the medium term, including:

General Balances

The risk is that the general reserve is not sufficient. This is mitigated by:

- The projected balance on the general reserve as at 31 March 2012 of £16.625m is 5% of the gross revenue budget requirement for 2008/09; and
- Strong financial controls have resulted in a consistent trend of the revenue outturn being delivered within budget in recent years.

Pay Increases

The risk is that pay increases may exceed the levels provided for within the MTFs. On the 15th October 2008 Police Officers agreed a three year pay settlement worth 2.65% in 2008/09 2.6% in 2009/10 and 2.55% in 2010/11. These awards have been factored into the indicative budget forecasts.

Price Increases

The risk is that price increases may exceed the levels provided for within the MTFs. Every 0.1% increase in prices will add £0.09m to the 2008/09 base budget. This is mitigated by:

- The non pay elements of the MTFs have been increased annually by 2.5% on the basis of the best available evidence; and
- The devolved element of the budget is generally controllable and encourages savings at a local level, and any under/over spends are transferred to/from devolved budget reserves.

Capital Financing

The risk is that Capital Financing charges will be greater than forecast. This is mitigated by:

- Revenue implications are considered as part of the capital planning process and
- Although the level of interest is subject to change, any change in the variable rate will have minimal effect as 100% of debt is at fixed rates.

Financial Planning

The risk is that a major liability or commitment is currently known but has not been taken into account in the financial planning of the Authority. This is mitigated by:

- The MTFs includes growth items classified on the basis of priority, to be assessed for inclusion in the Authority's budget, identified by the Chief Constable by reference amongst other sources to the Local Policing Plan; and
- Regular liaison by senior officers of the Force and the Authority and the existence of the Chief Officers Policy Group help to strengthen and coordinate the financial planning of the Authority and Chief Constable.

National Funding

The risk inherent in being below the floor for formula grant. This risk is not mitigated, but the funding levels for the first two years of the current MTFS have been provisionally agreed, confirming that the floors will remain in place, which gives greater certainty in the medium term. Were this position to change following CSR10, for example if floor increases were reduced to 0% over the period of the next CSR, options such as representations to Ministers to support an increase in the precept above 5%, and a full reassessment of reserves would have to be considered.

Loss of Deposit

The risk is that funds deposited by the Authority are lost due to the collapse of the financial institution with whom the deposit is placed. This risk is limited by the controls in the Treasury Management Strategy which focus on control of deposit rather than returns. The potential impact is limited by the strategy of a diverse portfolio with top rated institutions.

Interest Rates on Deposits

The risk is that interest rates will be lower than expected. This risk is mitigated by regular review, monitoring and reporting on interest rates. Prudent assumptions on likely interest rates for 2009/10 onwards have been incorporated into the MTFS.

Capital Programme Implications

The risk is that the capital programme may be understated, funding will not be available as planned, or that over spending may occur. This is mitigated by:

- Review of Estates Strategy reported in December 2008 together with quarterly updates of progress will provide assurance in the accuracy of forecasts;
- Quarterly capital monitoring reports to Resource Management Committee; and
- Prudential regime gives added flexibility in terms of financing the Capital Programme.

Risk Management

The risk is that all risks have not been identified in the MTFS and that major financial consequences may result. This is mitigated by:

- Risk management arrangements;
- Comprehensive self and external insurance arrangements in place;
- Adequacy of the insurance reserve; and
- Adequacy of the general balances and the overall reserves policy.

14. Conclusion

- 14.1 The analysis set out in the MTFS suggests that all of the options available to close the funding gap will need to be considered by the Authority to allow the current budget commitments and growth proposals to be delivered.
- 14.2 During the period of the MTFS to 2012, the Authority's reserves will reduce as they are used to support both revenue and capital priorities. Ongoing reliance on reserves in the longer term will need to be reduced as the planned efficiency savings are realigned.
- 14.3 Maintenance of the current system of floors and ceilings, with a guaranteed minimum funding level, should allow the Authority to fund proposed spending over the medium term without the need to make representations to Ministers on relaxation of the current council tax capping arrangements.
- 14.4 Further funding options, including council tax precept increases, will need to be considered over the next two months that will allow a balanced budget to be considered by members in February 2009.