

Open Report on behalf of Pete Moore, Executive Director of Finance and Public Protection

Report to:	Overview and Scrutiny Management Committee
Date:	24 November 2016
Subject:	Financial Standing of the County Council in Advance of the 2017/18 Budget Cycle

Summary:

This report provides an estimate of the budget shortfall being faced by the County Council over the next three financial years in the wake of the acceptance of the four year funding deal from Government. In so doing it provides the foundations for the forthcoming budget cycle and has recently been provided to all councillors in preparation for the Scrutiny Committee budget workshops that are now underway.

Actions Required:

The Overview and Scrutiny Management Committee is asked to consider the report and agree any comments to be passed onto the Executive Councillor responsible for Finance for consideration when making the budget proposals for next year.

1. Background

1. A series of confidential budget workshops for each Scrutiny Committee will be held over the months of November and December 2016. At the specific request of the Scrutiny Chairmen a short briefing note on the overall budget position of the Council going forward into this budget cycle was requested instead of a presentation on the subject at the beginning of each session. This report sets out the contents of this briefing note to councillors for discussion at the Overview and Scrutiny Management Committee.
2. The County Council at its meeting on 16th September 2016 agreed to accept the 4 Year Funding Deal offered by Government for financial years 2016/17 to 2019/20. This establishes the funding contribution from Government for these four years. This is summarised in the table below. Not taking the deal risked the real possibility of an even poorer funding position going forward. The vast majority of local authorities have accepted the deal.

Funding Summary	2016/17	2017/18	2018/19	2019/20
	£'m	£'m	£'m	£'m
Revenue Support Grant	70.351	48.292	33.964	20.139
Transitional Grant	0.011	0.009	0.000	0.000
Rural Service Delivery Grant	6.892	5.565	4.281	5.565
Top Up Grant	82.426	84.047	86.526	89.292
TOTAL	159.680	137.913	124.771	114.996

3. Despite the 4 Year Deal being in place it is presently felt as sensible to only set a one year budget as part of the coming budget cycle. It is not felt appropriate to bind the new post-May 2017 Council into a series of long term savings proposals set now when circumstances may change materially over the medium term. These circumstances are in part illustrated by the assumptions described later in this report which are the basis of the projections for the future funding shortfall of the Council.
4. The analysis presented later in this report provides an estimate of the budget shortfall the Council faces for the next three financial years. To derive such an estimate requires the making of a whole series of assumptions.
5. It is not legal to set an unbalanced budget so the shortfall must be found. The budget shortfall can be bridged by a combination of spending reductions, the use of reserves and the generation of additional income. The use of reserves can only be a temporary measure as they are a finite resource. More information on reserves is given later in this report.

THE SHORTFALL

6. The projected budget shortfall for the next three years is outlined in the table below together with the estimate of unavoidable cost pressures which, along with the funding reductions described in the table above, have fed into the derivation of the shortfall. To give these figures some context the current year net revenue budget is £445m.

	2017/18	2018/19	2019/20
Unavoidable Cost Pressures included in the shortfall below	£14.9m	£13.5m	£6.4m
Budget Shortfall	£57.4m	£74.1m	£75.5m

7. For clarity what this is saying is that there is a £57.4m shortfall at present in next year's budget which, if not addressed, rises by a further £16.7m to £74.1m in the year after and, again if not addressed, by another £1.4m to £75.5m in 2019/20. Again, for clarity, base budget savings approved for next year will also reduce the budget shortfall in the two subsequent years.
8. The main budget pressures comprise the following (figures relate to next year):
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| • Adult Care demography and minimum wage increase | £8.5m |
| • Increase in the number of Looked After Children | £1.8m |
| • Waste Disposal (volume and price impact) | £1.0m |
| • Microsoft licences | £1.4m |
| • County Elections (one year only) | £1.1m |
9. As mentioned the estimates of the shortfall have been made by making a large number of assumptions. The key ones are explained below:
- The four year funding deal as recently approved by full Council is delivered by the DCLG in line with that offered in the 2016/17 final local government grant settlement.
 - Already approved savings approved in previous years and already identified cost pressures materialise as presently predicted.
 - Council tax will increase by 3.95% pa for each of the 3 years covered by this projection. This implicitly assumes a referendum threshold of at least 2% for the non-adult care precept.
 - The tax base will grow by at least 0.75% pa every year for the next three thereby generating additional council tax revenue (a 1% increase in the tax base equates to £2.5m pa additional income). Whilst modest by comparison to recent growth of over 2% pa, the latter is more driven by the reducing demand for council tax support benefit than by new homes coming on stream. National changes to the welfare regime in tandem with above inflation increases in council tax risk increasing demand for council tax support thereby reducing future growth in the tax base.
 - The impending introduction of a national funding formula for schools implies it will no longer be possible to charge the Dedicated Schools Grant a £3.9m pa contribution towards the capital programme to reflect historic borrowing related to schools capital expenditure.
 - The Better Care Fund (BCF) as presently constituted will provide £15.9m pa every year of the three year period in direct contributions from Health.
 - The new improved BCF as announced in autumn 2015, and directly payable to the Council, will be fully available to the Council with any underlying conditions satisfied.

- Pay inflation is limited to 1% pa each year and there is no provision for price inflation other than use of the revenue contingency budget.
 - A technical change is made to the way in which the minimum revenue provision (MRP - part of capital financing charges) is calculated freeing £2m pa in revenue budget. Further scope for reducing the revenue costs in this area is underway and will be concluded shortly.
 - The new 3 year concession to use capital receipts to fund revenue costs of transformation change activity funds annual redundancy costs of £2m to £4m pa thereby freeing up the revenue budget allocation in those years. It is already assumed £8m of revenue (£2m to £4m relating to redundancy costs) can be substituted by capital receipts. Capital receipt generation over the 3 years in question could be as high as £40m leading to the potential for further substitution of revenue spend with capital receipts over the short term.
 - The general reserve remains at 3.5% - the upper end of our self-prescribed range.
10. Should any of the above assumptions be incorrect then this will impact on the budget shortfall. Indeed this aspect is one key reason for only setting a one year budget now but to continue to plan for the medium term outlook.
11. The proposed budget strategy for next year is to use a combination of budget reductions and reserves to bridge the £57m shortfall. In that regard it may be helpful to set out the position regarding the revenue reserves of the authority and, more specifically, the reserves that are available to assist in balancing the budget in the short term.

RESERVES

12. The 31st March 2016 financial statements of the Council show that it has a General Reserve balance of £15.6m and Earmarked Reserves of £150.2m. The former represents only 3.5% of the annual budget requirement and is funding of the last resort and cannot prudently be committed to supporting the annual budget. The level of this reserve needs to be maintained between 2.5% and 3.5% of the annual budget requirement as dictated by our County Council approved Financial Strategy. Earmarked Reserves can be categorised as follows:
- Money held by the County Council on behalf of schools but not within our control in terms of spending it - £26.6m.
 - Grants and contributions from Government and other bodies for specific purposes which, if not used for that purpose, have to be returned. These total £49.3m with major components being the BCF and related adult care funding (£27.8m); Growing Points (£4.5m); Schools (£7.6m); Public Health (£2.7m) and Children's Services (£6.3m). Historically these sums

would have been treated as creditors and not reserves but recent updates to accounting standards have required their reclassification as reserves.

- That leaves £74.3m in earmarked reserves directly within the control of the Council. Of this sum £43.8m is in the Financial Volatility Reserve with £20.2m of this committed to balancing the current year's budget. The balance of £23.6m is available to assist in future years in terms of supplementing the budget. This leaves £30.5m which can be summarised as follows:
 - Temporary reserves to facilitate the carry forward of Directorate 1% underspends from 2015/16 - £4.3m.
 - Health & Wellbeing reserve in which Health have a say in its use - £1.2m.
 - Insurance reserve held against known or expected claims given the high level of self-insurance undertaken - £6.4m.
 - Adverse weather reserve (gritting/other highway damage) - £1m.
 - Shared Services reserve (legal and procurement) with a portion of this owned by participating Districts - £2.1m.
 - Around 30 small service specific reserves - £15.5m.

13. The necessity for, and sufficiency of, all Council controlled reserves is being critically reviewed as part of this budget cycle. It is anticipated that it will be possible to release around £5m of currently earmarked reserves for general use.

CAPITAL

14. In terms of the capital programme there is provision for all currently approved schemes and annually reducing block allocations for items where there is an ongoing need (eg. building repair & maintenance, IT refresh, fire vehicles & equipment). In addition, an annual contingency of £7.5m has been established to be bid against for any new schemes. Existing capital reserves are being critically reviewed to establish whether they can be applied to fund existing or new schemes instead of borrowing. Capital receipts will not be used to fund the capital programme during the next three years whilst the concession is available to use such funds for certain types of revenue spending.

15. The funding of the capital programme is being reviewed with particular attention being paid to the Minimum Revenue Provision (MRP) which relates to the setting aside of revenue budget to repay long term borrowing when it matures. Clear scope exists to change the basis of provision to save

revenue budget in the short term, albeit at a potentially greater long term cost. The outcome of this review will be fed into the budget cycle.

TIMETABLE

16. The 2017/18 budget timetable going forward is as follows:

- November/ December 2016 – Scrutiny Committee workshops in closed session
- 23rd November 2016 – Autumn Statement
- Late November/early December 2016 – Provisional Local Government Grant Settlement
- 20th December 2016 – Executive agrees budget proposals as a basis for consultation
- January 2017 – Scrutiny Committees consider budget proposals in open session
- Mid-January 2017 – Formal consultation meeting with business, trade unions and public sector partners.
- Early February 2017 – Final Local Government Grant Settlement
- 7th February 2017 – Executive to consider consultation feedback and agree final budget proposals.
- 24th February 2017 - County Council considers budget proposals from the Executive.

2. Conclusion

The County Council faces a significant budget shortfall over the next three financial years and will need to address this situation by using a combination of budget reductions, income generation and the prudent application of available reserves.

3. Consultation

a) Policy Proofing Actions Required

n/a

4. Background Papers

No background papers within Section 100D of the Local Government Act 1972 were used in the preparation of this report.

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