

Committee	Executive Scrutiny Committee	
Date:	25 th January 2011	

Revenue and Capital Budgets 2011-12 and Beyond

1. Purpose of Report

- 1.1. To provide Executive Scrutiny with an overview of the revenue and capital budgets for 2011-12 and beyond.

2. The Provisional Settlement – National Position

- 2.1. After many months of debate and a steadily increasing volume of statements about the likely stringency of the Settlement, the Government announced the Provisional Local Government Finance Settlement, for 2011-12 and 2012-13 on 13th December 2010. This followed the Comprehensive Spending Review 2010 (CSR), which was announced on 20th October 2010. The CSR suggested an average of 7.25% per annum cuts to local government over the next 4 years, but with front loading of 10.7% in 2011-12. While the CSR covers a 4 year period, the provisional settlement is only for 2 years
- 2.2. It was also known that many specific and area based grants (ABG) were to be rolled up into the formula grant or lost altogether. Similar changes were also taking place with regard to Dedicated Schools Grant (DSG) with many specific schools grants being rolled into DSG. All of these changes and the lack of clarity about some of them, made predicting the outcome of the provisional settlement challenging, even without taking account of the vagaries of the four block formula grant model itself.
- 2.3. The provisional settlement followed the CSR pattern through stating that nationally, excluding Police Grant, formula grant will be £24.9 billion in 2011-12 and £22.9 billion in 2012-13. This compares to an adjusted 2010-11 base of £28.3 million, hence a 'raw' reduction of 10.2% between 2010-11 and 2011-12 and a further 5.9% to 2012-13.
- 2.4. In order to attempt to mitigate some of the worst impacts of the reduced grant funding, 'transition grant' was introduced to protect those authorities most

dependant on grant funding. In order to allocate transition grant, the Government used a new calculation of “Revenue Spending Power” to judge the movement in funding between years, a measure which includes council tax, formula grant, specific grants and new funding directed through the NHS to support social care and benefit health. As part of his Settlement speech to the House of Commons, the Secretary of State for Local Government, Mr Eric Pickles, stated that no authority would face more than an 8.9% reduction in spending power in either 2011-12 or 2012-13.

- 2.5. Over £4 billion of other grants have been rolled into formula grant and ring-fencing of most revenue grants, except some schools grants, has been removed for 2011-12 and 2012-13.
- 2.6. The Government is providing £1 billion of additional funding through the NHS budget to support joint working between the NHS and councils. In addition, Personal Social Services grant for social care has been increased by £1 billion to £2.4 billion a year by 2014-15, rolled into formula grant.
- 2.7. The Council Tax Freeze grant is a new funding heading across each of the four years of the spending review, to protect council tax payers by enabling councils not to increase Council tax in 2011-12. While the heading is new, the cash comes from the existing grant allocation.
- 2.8. The removal of ring-fencing of grants is generally welcomed by local government. However, with significant numbers of grants being rolled into formula grant, many authorities have been seriously affected by the distributional effects of the four block model used to allocate formula grant.
- 2.9. Government has also implemented a more complex floor arrangement compared to previous years, with the floor position being judged according to the ability of the authority to raise funding locally through council tax. There are four bands as illustrated in the table below, with Essex County Council falling into Band 4. This means that Essex County Council can lose the maximum before protection applies due to our perceived ability to raise council tax – see comment below (para 6.4).

	2011-12	2012-13
Grant 'floors' (minimum grant increases) for Education and Social Care authorities:		
Band 1	-11.3%	-7.4%
Band 2	-12.3%	-8.4%
Band 3	-13.3%	-9.4%
Band 4	-14.3%	-10.4%

3. Impact of the Provisional Settlement on Essex County Council

- 3.1. Essex County Council's allocation of Formula Grant for 2011-12 is £284.0 million. This compares to an adjusted 2010-11 base of £324.0 million, a reduction of £40.0 million, -12.4%. ("Adjusted base" means the 2010-11 allocation adjusted to reflect any grants that are rolling into or out of formula grant, or any changes to methodology, to provide a like-for-like comparison between years).
- 3.2. After the Comprehensive Spending Review (CSR), Essex County Council had been planning for formula grant in 2011-12 of £302.6 million based on the same proportionate share as for 2010-11. The headline allocation of £284.0 million meant that we had to find an additional £18.6 million of savings for 2011-12.
- 3.3. Government only announced two years' settlement information and for 2012-13 the situation was slightly worse with our previously modelled formula grant of £290.5 million comparing to an allocation of £260.4 million, a gap of £30.1 million.
- 3.4. Following the implementation of the new floor arrangement, Essex County Council falls into band 4 which assumes most ability to raise local funds and hence has received a lack of support from the floor mechanism. Furthermore, as we are above the floor, we have had £15.7 million removed from our funding to support authorities who would otherwise fall through the floor.
- 3.5. Essex County Council also applied for capitalisation of redundancy costs, following an invitation by CLG to bid for this for 2011/12 only. Regrettably the application was unsuccessful,. As a result the severance costs will be a further burden on the budget in the year in which they fall.
- 3.6. Schools and other services supporting the operational provision of learning for school aged pupils and students are funded from a range of specific grants: the Dedicated Schools Grant (DSG); Specific Grants; and (for 16-19 year olds) the Young People's Learning Agency (YPLA). The DSG is the major funding source. The government has decided that specific grants will be "mainstreamed" into DSG from 2011-12.

The Table below highlights the impact on DSG of mainstreaming specific grants:

Year	Amount per pupil (GUF)	Pupil Numbers	Gross DSG £000	Academies deduction £000	DSG remaining with LA £000
2010-11 (updated)	£4,237.80	191,769.4	812,680	(28,120)	784,560
- specific grants	£578.43		110,926	(4,419)	106,507
2011-12 (estimate)	£4,816.23	191,769.4	923,606	*(52,270)	871,336

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*the 2011-12 Academies deduction relates to the schools which have or will have transferred to Academy status by 31 March 2011. Numbers change on a monthly basis as more schools opt to transfer.

3.6.1. There has been no increase in school funding per pupil, year on year, and there is unlikely to be any increase in per pupil funding through 2011-15.

3.6.2. The Schools Forum is reviewing how specific grants might be distributed to schools in 2011-12.

3.6.3. Final DSG 2011-12 will be determined following the schools' January Census; numbers will be available mid to late February.

3.7. The government will introduce a new Pupil Premium in 2011-12 which will increase to £2.5 billion nationally by 2014-15. Resources will be delivered to schools in 2011-12 on the basis of the numbers of 4-15 year olds with a Free School Meal Entitlement at a rate of £430 per pupil. Further, the premium will support Looked After Children at the same rate and children from a military background at £200 per pupil. It is anticipated that Essex schools will receive between £8 million and £10 million in 2011-12.

4. Mitigating Actions Taken to Address the Budget Gap

4.1. The Council has been preparing information for the future years' budgets since July 2010, against a back drop of predicted stringent financial constraints. The transformation programme, already in progress, has assisted considerably in managing in this environment.

4.2. A number of bilateral portfolio meetings took place over August and reviewed progress towards achieving cash reduction targets. This meant that we were largely prepared for the Comprehensive Spending Review (CSR) 2010 announcement on 20th October and the Council had a significant amount of information about its own circumstances from which to react.

4.3. Following our interpretation of the CSR but before the settlement, we had calculated that the Council needed to find £132 million of initiatives (savings, efficiencies and service reductions) to set a balanced budget. This was to offset £123 million of new service pressures and reductions in or removal of specific grants and £9 million to offset estimated formula grant reductions (before the impact of formula grant variations).

4.4. A significant number of initiatives were identified to close this estimated gap

- 4.4.1. Thorough review and analysis of reserves –reducing Service Improvement / Transformation Reserve, reprofiling the replenishment of Waste Reserve, removing Developing Partnership Reserve. This review was to continue post-settlement.
 - 4.4.2. Critical analysis and review of some pressures and savings – to provide assurance around the rationale applied to pressures and to ensure savings plan will deliver in full and on schedule
 - 4.4.3. Risk analysis and review – to ensure appropriate approach to risk is applied across the council and to identify and highlight risk as included in the forecast budget position
 - 4.4.4. Critical analysis of transformation projects to ensure the same approach is applied to capturing and accounting for all projects. Also a review to ensure robust delivery plans are in place for all projects and to monitor delivery on schedule
- 4.5. We were clear however, that we needed to wait until we received our specific settlement, expected in early December, to fully understand the Council's overall position.
- 4.6. After the Provisional Settlement, with the knowledge that our estimated gap had been increased by a further £18.6 million, a further review and analysis of reserves was carried out and new initiatives considered. The gap was closed through:
- 4.6.1. Further adjustments to the Waste Reserve, but ensuring that payback occurs to deliver the target by 2014-15 in order to mitigate potential council tax increases in that year and beyond.
 - 4.6.2. Ensuring that any new funding sources are applied to existing service commitments as a priority, before undertaking new commitments.
 - 4.6.3. Reduction of the capital programme and the resultant impact on the capital financing requirement
- 4.7. The £300m Transformation Programme represents our desire to take control of our financial destiny by ensuring we operate as a joined-up, customer focussed organisation. The process has helped us to understand in more detail the costs of the services we provide, in order for us, as one council to better meet the needs of stakeholders with the resources we have available.
- 4.7.1 The Transformation Programme has been helping support the need to drive a more streamlined & efficient way of delivering valued services to our stakeholders. This has been a considerable undertaking in changing the way the organisation thinks about service provision, the costs

associated with delivering these services and challenging us to ensure we are receiving value for money for the services we deliver.

4.7.2 The Transformation Programme has been initiated to ensure consistent change is understood, managed and governed appropriately throughout Essex County Council. To pump prime this large scale proactive change programme it has been necessary to draw down from reserves. The longer term alignment of objectives and budget stability are the key deliverables of the Transformation Programme.

4.7. As a result of the effort expended to draw up a balanced budget, the following figures were produced, showing a budget requirement of £876.6m for 2011-12 and £870.5m for 2012-13

	2011-12 £000	2012-13 £000
Original Net Budget (as submitted Feb 2010)	904,094	904,094
New Pressures	77,789	115,789
Savings and Efficiencies (Services)	(108,134)	(179,008)
Budget Requirement before Reserve Movement / Financing	873,749	840,874
Reduced Contribution to Waste Reserve	(24,150)	(9,381)
Movement in Other Reserves	27,002	38,960
Forecast Budget Requirement	876,601	870,454

5. Robustness of the Budget

5.1. Assessment of Risks

- 5.1.1. Although best estimates have been taken into account when compiling the budget, the nature of the services provided by the Council means that there will always be a level of financial risk which needs to be monitored and managed.
- 5.1.2. Risks have been quantified based on the Corporate Risk Scoring Guidelines using a 4x4 matrix. The matrix assesses likelihood and impact of any event occurring, with the highest scores indicating the highest level of risk.
- 5.1.3. In 2011-12, these significant savings and demand risks have been assessed as having a value of £30 -£35 million.

5.2. Steps to Minimise and Manage Risk

- 5.2.1. In building the budget, the authority has considered the risks inherent within it and has mitigated these as follows:
 - 5.2.1.1. The consideration of specific service contractual obligations which may not conform to general inflation levels.
 - 5.2.1.2. The on-going impact of the Schools, Children and Families improvement programme.
 - 5.2.1.3. The reflection of lower interest rates on the investment returns and borrowing budgets. 1% change in investment returns implies an estimated movement of £343 million in the budget, while a 1% change in borrowing costs implies an estimated movement of £1,590 million.
 - 5.2.1.4. Only using capital receipts that have been realised to finance the capital programme.
 - 5.2.1.5. It is assumed that pay awards will continue to be low, and no additional financial provision has been made. A 1% pay increase across all staff, for example would cost £2.4 million.
 - 5.2.1.6. In addition, the authority has a number of processes embedded within its day to day working to minimise, and manage its risks, including:
 - 5.2.1.7. Promoting a robust approach to financial planning with services, looking at both the near and longer term.
 - 5.2.1.8. Use of performance reporting and balanced scorecards to act as an early warning system.
 - 5.2.1.9. Regular reporting to Members of the projected outturn, including outlining remedial action where appropriate – the quarterly reports

to Cabinet are also considered by the Audit and General Scrutiny Committee.

- 5.2.1.10. An established system of financial management, culminating in the presentation of monthly reports to the Corporate Leadership Team.
- 5.2.1.11. The operation of a risk management approach as set out in our Risk Management Policy and Strategy: Prudence, Strength and Performance.
- 5.2.1.12. The presence of the Council's internal control framework, including the Financial Regulations and Schemes of Delegation for Financial Management which provides the framework for delegated budget management.
- 5.2.2. Many other processes exist however, it has to be recognised that these steps will not serve to eliminate risk entirely, especially for those that come from external sources, such as the demand pressure for social care support, and price fluctuations beyond those already included in the budget. There are further measures that can be taken to diminish the overall financial effect of these risks:
 - 5.2.2.1. Slowing down or stopping spending or increasing income elsewhere in the organisation. The greater the extent that this is possible, the lower the overall impact of risks.
 - 5.2.2.2. The extent to which it is possible to move funds around the organisation, and so utilise savings in one area against pressure in another.
- 5.2.3. The authority has demonstrated its ability and willingness to take the above steps in the past when it has been necessary.
 - 5.2.3.1. The Council's insurance arrangements – the overall budget and insurance provision allow for estimated excesses on claims and costs that fall to the council.
 - 5.2.3.2. The level of the council's emergency contingency, which is set at £8 million.
- 5.2.4. A further source of funding is, of course, the Council's reserves and balances.

5.3. Reserves and Balances

- 5.3.1. Reserves provide for mitigation of the level of risk inherent in building a budget in times of financial constraint. As well as providing for the future we know that balancing our budget requires innovative savings plans which may suffer delays, for example. Our reserves are essential to cushion services against shortfalls.
- 5.3.2. We have built up acceptable and reasonable levels of reserves so that the authority can continue to deliver services, even in the advent of financial

shocks. Our budget process has made use of reserves to ease the financial pressures but this had to be done in a responsible and sustainable way.

- 5.3.3. Many of the reserves e.g. Waste, PFI and Insurance are earmarked to enable us to afford to pay our bills in future years without further impacting the council tax - i.e. we are saving today for the rising costs of tomorrow to smooth costs. This is prudent and well thought through.
- 5.3.4. The Waste Reserve, in particular has been set up by Essex County Council to smooth the year on year increase in waste disposal costs arising from EU legislation re landfill limits. This was exemplary forward prudent planning by the authority which has won us praise from central government project assessors.
- 5.3.5. Raiding the reserves is not a long-term sustainable policy as they soon run out and in any case, ongoing revenue funding requirements should not be funded from one-off sources. Consequently any 'borrowing' from reserves is budgeted for pay back in later years.
- 5.3.6. We have made use of reserves to fund invest to save (transformation) projects. This is a good example of where we are using one off money to fund one off expenditure and then paying back from the savings that ensue. In addition, we are being very flexible about the payback period to ensure the strain on individual years is not too great and current expenditure on key services is protected as far as is possible

6. Capital Programme

- 6.1. In a welcome move from Central Government, both the Department for Transport (DfT) and the Department for Education (DfE) have provided 100% capital grants to support the capital programme. These grants are a mixture of ring fenced and non ring fenced thus allowing the authority some flexibility in how to use the grant awarded.
- 6.2. In the last three year settlement, there was a noticeable shift in the proportion of grants to supported borrowing and this appeared to be recognising that Local Authorities needed cash grants not revenue funded borrowing. This trend has been continued in the 2011-12 allocations. The indicative figures for future years imply that this will be sustained for the following three years.
- 6.3. The level of funding from DfT was a little lower than the previous years' as the integrated transport block was reduced by a third. The DfE allocations were significantly reduced as programmes either ended i.e. Extended schools, significantly reduced like the Primary Capital Programme or were removed.

- 6.4. ECC's provisional capital programme totals are as follows: £231.456 million in 2011-12, £126.015 million in 2012-13 and £101.550 million in 2013-14.

Analysis of grant and supported borrowing awarded by central government departments			
	2010-11	2011-12	2012-13
	£000	£000	£000
SCE (R)	51,546	-	-
Grant	234,040	159,274	90,387

7. Future Years – Medium Term Financial Plan (MTFP)

- 7.1. As explained earlier in this report, the Government has only announced two years' settlement information, for 2011-12 and 2012-13. In his Local Government Settlement speech on 13th December, Eric Pickles, the Secretary of State for Communities and Local Government, announced this settlement as a transitional one, using an inherited system. He said that in providing details for the next two years he was aiming to strike a balance between the need to help councils plan and the need to reform the system.
- 7.2. As a result, whilst considerable work has been undertaken on the 2013-14 budget, there remains some uncertainty over the resources available. Consequently, there are no funding figures shown in the table as they cannot be predicted with any certainty.

	2011-12 £000	2012-13 £000	2013-14 £000
Original Net Budget (as submitted Feb 2010)	904,094	904,094	904,094
New Pressures	77,789	115,789	150,465
Savings and Efficiencies (Services)	(108,134)	(179,008)	(229,515)
Budget Requirement before Reserve Movement / Financing	873,749	840,874	825,045
Reduced Contribution to Waste Reserve	(24,150)	(9,381)	48,350
Movement in Other Reserves	27,002	38,960	28,960
Forecast Budget Requirement	876,601	870,454	902,355

- 7.3. There are two notable features in regard of the figures above for 2013-14, in addition to the continuing pressures and transformation / efficiency programmes. Firstly 2013-14 sees a planned substantial payback of the Waste Reserve of the amounts 'borrowed' in 2011-12 and 2012-13. This is to restore the Reserve to the level required to sustain waste expenditure in future years.
- 7.4. Secondly, as indicated above, the provisional settlement is only for two years, hence the funding for year 3, 2013-14, is far from certain. While we have an indication of the national funding figure, it is known that CLG is reviewing the funding formula. It is anticipated that further information on this review, and exemplifications arising from it, will emerge in 2011.
- 7.5. As a consequence of the pressures, efficiencies, capital programme adjustments and payback of reserves the projected budget 2013-14 is approximately £902.4million
- 7.6. During the budget process the authority has been careful to act in a measured way to predict funding shortfalls, ensuring that robust plans are in place. Consequently, the authority is taking the following mitigating measures to address the projected funding shortfall in 2013-14:
- 7.6.1. Continuing delivery of the transformation programme, especially the 'New Ways of Working' series of projects, which facilitate a more efficient way of delivering valued services.
 - 7.6.2. Reviewing planned commitments against the Waste Reserve to identify if replenishment can be delayed without jeopardising the ability of the Reserve to support the long term waste project;
 - 7.6.3. Continuing to make representations to CLG on the funding formula to ensure that it reflects Essex County Council's circumstances, that floor projection is properly funded and that area cost adjustment is protected;
 - 7.6.4. Maximising income across all services;
 - 7.6.5. Ensuring that appropriate operating models are deployed in both front line and back office services to reduce costs while protecting services to the public;
 - 7.6.6. Reviewing the capital programme in terms of quantum and funding sources to seek to reduce the impact on the revenue budget
- 7.7. While it is disappointing that the CLG has not been able to declare provisional funding settlements across all years of the CSR, from the point of view of financial planning, it is hoped that a fundamental review of the four block model will produce a more transparent, stable and equitable methodology for funding allocation. Meanwhile, Essex County Council will continue to push forward its Transformation Programme to ensure that it is best placed to effectively assess the impact of future settlements, and wherever possible does not have to react with short term savings measures.