

Scrutiny Committee Report



Listening Learning Leading

Report of Head of Finance

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AGENDA ITEM 6

2012/13 budget update report

Purpose of report

1. The purpose of this report is to inform the scrutiny committee of the budget target for 2012/13 and the composition of the base budget, to set out the issues to be considered by councillors before council sets a revenue and capital budget for 2012/13, and to report on 2012/13 government funding.

Background

2. In February 2012 cabinet will consider a report on the revenue and capital budgets for 2012/13 and will recommend 2012/13 budgets to council. To allow councillors to make informed recommendations all relevant issues affecting funding, expenditure and income must be brought to their attention in a timely manner to allow them an opportunity to challenge and consult on the options available.
3. This report considers revenue and capital income and expenditure and funding options available, paying particular attention to those areas where councillors have significant discretion over the outcomes.
4. In preparing the revenue and capital budgets the council must have regard to the Medium Term Financial Strategy (MTFS) considered by cabinet on 8 December 2011 and agreed by council on 15 December 2011. This sets out a number of objectives to be achieved and a set of principles to be followed in the preparation of budgets.

Revenue budget 2012/13

Budget target 2012/13

5. The MTFFS approved by council on 8 December 2011 sets a target within which the revenue budget will be set each year. It is:

'to set a revenue budget requirement that increases by no more than inflation each year, except where new responsibilities are placed on the council'.

6. To meet this objective the budget must be set within the budget limit for 2012/13. This has been calculated in **appendix A table 2** as £13,874,794, representing the budget requirement for 2011/12 (£13,066,755) as adjusted for inflation, and new responsibilities.

Base budget composition 2012/13

7. The starting point for building the base budget 2012/13 is the 2011/12 base service budgets for service teams, of £15,860,787, plus the budget contingency of £300,000. This has then been updated for the following:

- opening budget adjustments, including the removal of one-off growth items relating to 2011/12
- addition of
 - inflation, salary increments and other salary adjustments
 - essential growth
 - new responsibilities
- removal of costs relating to
 - base budget savings
 - Fit for the Future (FFTF) savings
- growth proposals
 - one-off and ongoing growth

to produce a budget requirement for 2012/13 of £12,119,230.

8. This budget represents the budget proposals submitted by officers and it affords resources to allow the council to provide services at the current standards (all other things being equal), and reflects previously agreed policy decisions. It also includes essential growth items, any growth in respect of new responsibilities placed on the council, and all growth proposals which have been put forward by officers.

9. The 2012/13 figures are provisional and are liable to change as work continues on refining the budget. The paragraphs below identify how the budget requirement for 2012/13 has been reached.

2012/13 budget build changes

10. **Appendix A table 1** summarises the movements in the base service budgets of £15,860,787 for 2011/12 and the 2012/13 cost of services amount of £15,396,639. The following paragraphs detail these movements.

Opening budget adjustments (appendix A note 1)

11. A total of £1,150,481 is removed from the base budget for one-off items (£924,923) agreed in previous budgets, and the realisation of the full-year effect of savings proposals identified in previous years (£225,558).

Inflation, salary increments, and other salary adjustments (appendix A note 2)

12. Together these total £195,113. The inflation figure of £392,498 represents an average increase of just under three per cent on the 2011/12 net expenditure budgets. For all council employees, except for the chief executive, strategic directors and heads of service, an increase in salary of two per cent is budgeted for 2012/13. Increments payable to council employees not at the top of their salary range total £77,433. Other salary adjustments represent a net saving of £274,818 reflecting additional savings arising from restructures initiated in prior years and other budget corrections.

Essential growth (appendix B)

13. These items total £375,140. They comprise additional expenditure which is considered unavoidable, and reflect changes that have occurred in the current year or which are known will happen in 2012/13. Given the value of these additional essential growth items they are subject to further review.

Changes in responsibilities

14. There are no costs relating to changes in responsibilities in 2012/13

Base budget savings (appendix C)

15. These items total £373,640. These base budget savings are reductions in costs identified by officers which may be the result of more efficient working or previously agreed policy decisions, cost reductions outside of the council's control, or correction to budgets

Fit for the Future savings

16. On 6 December 2007 cabinet agreed to approve the proposal to use a lean systems thinking approach to remove inefficiencies in business processes and improve the quality of customer service. Internally this approach is badged as Fit for the Future (FFTF).
17. The fourth phase of this project will commence shortly and involves processes in some of the council's service teams being looked at in detail with the aim of identifying efficiency savings. The provisional savings targets are summarized in table 1 below. The cabinet will have to take these into account when recommending its budget to council.

Table 1: FFTF savings targets (cumulative)

Year	£
2012/13	50,000
2013/14	110,000
2014/15	186,500
2015/16	186,500

Revenue and capital growth

18. In setting the annual budget the council must consider if it wishes to enhance, improve or extend existing service provision. Heads of service have submitted a number of suggestions for additional spend that support the council's key aims as set out in the council's corporate plan, and management team has agreed that a number of these merit further consideration as part of the budget setting process.

19. These proposals are included in the base budget but they are still under consideration and are subject to political decision as to whether they will be included in the formal budget proposals. Although inclusion of the growth bids in the base budget increases the council's budgeted expenditure, the council could include one or more of the growth items in the revenue budget for 2012/13 or the capital programme without increasing the council's budgeted expenditure by funding growth proposals that are one-off from the enabling fund (this is assumed to be the case in the budget shown).

20. The growth bids are attached to the report as follows:

- **appendix D** – revenue growth bids - £228,720
- **appendix F** – capital growth bids – including net revenue ongoing costs of £11,000

21. It will be for the council to decide in February whether these or any other proposals are included in the final budgets. If any member of the committee wishes to have further details of any of the bids please can they contact the relevant head of service. As a result of all of these changes, the cost of services for 2012/13 is £15,396,639.

Investment income

22. In 2010/11 the council received £1.9 million in investment income. This was significantly down from £2.5 million earned in 2009/10. This was used as follows:

- £500,000 to support capital grants (CIF);
- £1,200,000 to support the revenue budget for 2011/12; and
- £200,000 reinvested in financial instruments.

23. Investment earnings for 2011/12 are available to finance expenditure in 2012/13 and are expected to be higher than earnings in 2010/11. It is currently forecast that £2.122 million will be earned in 2011/12. Interest rates are expected to remain low for the foreseeable future, as shown in table 2 below:

Table 2: projections of future interest

	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
	£000	£000	£000	£000	£000	£000
Average balances	94,486	90,067	85,928	77,372	70,303	67,092
Working capital	15,000	15,000	15,000	15,000	15,000	15,000
Estimate of average balance in year	109,486	105,067	100,928	92,372	85,303	82,092
Forecast average interest rate	1.94%	1.86%	2.25%	2.50%	3.00%	3.00%
Forecast interest earnings	2,122	1,954	2,271	2,309	2,559	2,463
Less unit trust income	(378)	(250)	(250)	(250)	(250)	(250)
Forecast distributable interest	1,744	1,704	2,021	2,059	2,309	2,213

24. The current base budget assumes that £0.5 million of the forecast distributable investment interest of £1.744 million expected to be earned in 2011/12 is used to finance capital grants, with the balance used to fund revenue expenditure in 2012/13.

Property income

25. Property income represents the council's income from its investment property portfolio, and is estimated at £1,150,030.

26. After taking investment and property income into account the net budget for 2012/13 is estimated at £13,002,609. The net budget is further reduced by the managed use of earmarked reserves and by charging certain sums to capital, as identified in the following paragraphs.

Charges to the capital programme

27. Where officer time is spent on capital projects the cost is charged to the capital programme. This is provisionally set at £20,000.

Use of reserves and other funding

28. Some of the essential growth items identified as forming part of the base budget are one-off, and therefore are eligible to be funded from the enabling fund. These costs total £220,150. New one-off growth schemes agreed for inclusion in the 2012/13 budget may also be funded from the enabling fund – this is assumed in the budget shown.

29. A contribution of £270,000 from the vacancy reserve has also been included - the same amount as the current year. This is from savings achieved on salary budgets in earlier years.

30. Council tax freeze grant of £343,229 is included. Paragraph 37 discusses this in more depth. New homes bonus grant funding of £606,240 is shown as received, but transferred to an earmarked reserve. This is discussed in more depth in paragraph 39.

31. Taking into account these contributions the provisional budget requirement for 2012/13 totals £12,119,230.

Capital programme 2012/13 to 2016/17

32. The capital programme has been reviewed in detail by heads of service in conjunction with finance staff as part of the budget monitoring process, and has been changed to reflect current expectations of the spending profile. An updated programme, reflecting these changes, is attached as **appendix E**. The movement in this current capital programme from the original programme agreed by council in February was discussed in the budget monitoring report to cabinet on 8 December 2011. The programme also includes a statement of how it will be funded.

Government funding for revenue expenditure

33. In October 2010, as part of the comprehensive spending review, government announced that councils would see “an average loss of grant of 7.25 per cent, in real terms, in each of the next four years¹”, i.e. 29 per cent over 4 years. In reality however, this council lost 15.2 per cent in the 2011/12 settlement and a further 13.2 per cent reduction this year meaning, the council will have lost 28.4 per cent in the first two years alone. Officers are expecting that over the four year period the council will actually lose 40 per cent.

34. The impact of the settlement on the council’s grant funding is shown in table 3 below:

Table 3: local government settlement 2011/12 to 2012/13

	2011/12 actual £	2012/13 provisional £
Formula grant after adjustment	6,038,448	5,238,594
Increase/(decrease) year on year	(1,081,802)	(799,854)
Percentage increase/(decrease) year on year	(15.2%)	(13.2%)
Cumulative percentage/(decrease) from 2010/11	(15.2%)	(28.4%)

Issues for consideration

35. The paragraphs below set out further issues that need to be considered before the final budget for 2012/13 is set by council in February 2012. As such they represent areas of discretion in the budget setting process that are open to councillors.

Setting the budget

36. As shown in **appendix A table 2**, the current base budget is within the budget target as set in the medium term financial strategy.

¹ Letter from secretary of state for communities and local government, October 20 2010

Council tax freeze grant

37. The government has announced that it will pay an additional grant to councils which do not increase their council tax in 2012/13. The grant will be the equivalent of a 2.5 per cent increase in council tax, which for the council would equate to an additional grant of £171,988. CLG has confirmed that this grant, if the council chooses to accept it, will be for one year only. In terms of tax yield, the council will be worse off in 2013/14 as a result of not increasing council tax. The council is already receiving a four year grant of £171,241 annually from the first tranche of the council tax freeze grant (2011/12 to 2014/15). Again in terms of tax yield, the council will be worse off in year 2015/16 as a result of this grant funding ceasing, than it would have been if council tax had been increased last year by 2.5 per cent.
38. If the council decides to reduce council tax by 2.5 per cent, ongoing receipts from 2012/13 will reduce by £171,988. In order to raise council tax in the future to the level of income currently received, council tax will have to rise by 2.56 per cent from the lower base level.

New homes bonus

39. As part of last year's settlement, the government announced a new homes bonus scheme, aimed at incentivising local authorities to increase housing supply by rewarding them with additional grant. As part of the 2012/13 settlement the council received £259,699 which the council budgeted to put into an earmarked reserve. This will be received for a further five years. This year, in addition to the £259,699, the council will receive £346,541 as part of the second tranche – a total of £606,241 for 2012/13. The council will need to decide how the additional funds received are to be used – it is currently assumed that the funding received will all be transferred to an earmarked reserve. The uncertainty surrounding the future funding of this bonus is considered further in paragraph 46.

Community Investment Fund (CIF)

40. Each year the council has to make an explicit decision regarding the use of income earned by the CIF. The income is revenue money that could be used to pay for either revenue or capital expenditure. In preparing the draft budgets, as discussed in paragraph 24 above, it has been assumed that £0.5 million is used to support capital grants, with the remainder being used to finance the revenue budget.

Uncommitted resources – earmarked revenue reserves

41. The estimated enabling fund balance at 1 April 2012 is £16.7 million. However, for the purposes of budget setting the relevant figure is the estimated uncommitted enabling fund balance after taking into account funding commitments (e.g. capital schemes) and projected earnings on investments. As at the 31 March 2017 it is estimated the uncommitted balance will be £3.3 million (Appendix G line 108).
42. This estimated balance assumes that all growth bids proposed in this report are accepted, and that the enabling fund is used to balance the revenue budget in future years where the council's budgeted expenditure exceeds its income. It also reflects the impact of the reduction in interest rates, which reduces the amount the council can expect to earn on its investments and then use to support the revenue account.

43. In setting its budgets the council has always budgeted at full establishment and as a result of vacancies has under spent. The council operates a vacancy factor reserve into which salary underspends are paid and from which a contribution is made to fund revenue expenditure. At 1 April 2011 the reserve stood at £1,660,000. In setting the 2012/13 base budget £270,000 has been taken from the vacancy factor reserve to fund the revenue account.
44. For a number of years the council has maintained a pension fund reserve. The reserve can be called on to smooth out the impact of rises in superannuation costs. The current balance of this reserve is £937,000. As part of last years budget setting process it was agreed not to use this funding to support the revenue account. In 2012/13 the council's superannuation costs will increase by £50,000 as a result of the stepped impact of the last triennial valuation.
45. As part of the 2011/12 budget, a "revenue budget smoothing reserve" was created to help ensure that in an environment of falling government funding, the council could keep council tax increases to a minimum. The value of the reserve will be £642,003 at 31 March 2012.

Future prospects

46. In addition to considering the budget for the 2012/13 financial year, consideration must also be given to the financial position of the council over the medium term. In particular, the impact of the likely continued reduction in government grant funding over the medium term will present a significant challenge for the council. There are three particular issues for which costs and potentially revenues will not be known until summer 2012 at the earliest, they are:
- Localisation of council tax benefit – consultation on this policy has recently closed with primary legislation expected in the summer of 2012. A 10 per cent cut in funding of this benefit is proposed, with pensioners and other vulnerable groups being "no worse off" as a result of the implementation of locally designed and administered local authority schemes. Claimants falling outside those protected groups may suffer cuts to benefits exceeding 20 per cent if local schemes choose not to subsidise the cut.
 - Business rates retention – consultation on this ended on 24 October 2011. Legislation is expected for implementation in April 2013. Instead of contributing all business rates into a central pool as is currently done, from a base line year, any "new" rates collected will be retained locally. Conversely if collection rates decline, there will be a negative impact on funding locally. The rationale behind the new strategy is to encourage authorities to use all means at their disposal to stimulate economic growth.
 - New homes bonus – although the grants awarded for 2011/12 and 2012/13 are known or can be estimated quite accurately, total grants awarded in excess of the £250,000,000 set aside by government for 2012/13 to 2014/15, will be funded from formula grant. This means that the new homes bonus is not new money for the council, but a redistribution of funding that will in time lead to a fall in formula grant funding, the impact of this is currently unknown. The

government has stated that “Those authorities which respond to the incentive and embrace housing growth will reap the benefits”².

47. On 16 February 2011, the welfare reform bill was introduced to parliament. The Universal Credit, a major feature of this bill, will be administered by the Department for Work and Pensions (DWP). It aims to simplify the current benefits system providing a basic allowance which will replace amongst other benefits housing benefit currently administered by local authorities. The potential implications and opportunities for local authorities are significant.
48. The DWP will hold further discussions with local authorities about the detail and implications of universal credit for their housing benefit operations, including consideration of whether there may still be a role for local authorities in dealing with non-mainstream housing benefit cases (for example, people living in supported or temporary accommodation). Local authorities may also have a role to play in delivering face-to-face contact for those who cannot use other channels to claim and manage their universal credit. The government’s timetable indicates that by April 2014 all new benefit claims will be made through universal benefit.
49. The government has completed consultation on proposals to decentralise responsibility for setting planning fees to local planning authorities.. The proposals will allow authorities to set planning applications fees on the basis of full cost recovery, if they wish. This will help reduce the local taxpayer subsidising the planning service. If the authority decided to recover costs in this way, there will be a significant increase in application fees.
50. Officers are currently waiting for the Regulations that will set out how the authority can set its own fees. The regulations and the setting of fees had been expected to be implemented from October 2011 but they have been delayed. When the regulations are released officers will work through the implications and report to cabinet. Cabinet will then need to decide whether and when it wishes to implement this change.
51. **Appendix G** of this report presents a Medium Term Financial Plan (MTFP) for the council, which quantifies the financial pressure on the council over the medium term. It assumes that government grant funding will fall in total by 40 per cent by 2014/15. It also incorporates assumptions on interest income, and other known pressures on the council, such as inflation and salary increments. In line with the draft corporate plan, it assumes no change to council tax for 2012/13 and 2013/14, with a two per cent increase thereafter. It does not however reflect the items in paragraphs 46 to 50 above, where costs and revenues are unquantifiable at the present time.
52. Based on current assumptions, the enabling fund will need to be called upon to set a balanced budget in future years. The projected use of the enabling fund is shown in table 4 below:

² New homes bonus: final scheme design DCLG February 2011

Table 4: use of the enabling fund to set balanced budget

	Ongoing savings required £000
2012/13	(272)
2013/14	1,253
2014/15	1,738
2015/16	2,513
2016/17	2,913
Total	8,145

53. As identified above, if base budget for 2012/13 was adopted as the budget for the year with no further changes then, based on the assumptions the council would need to use £8.145 million of reserves.

54. If the council were to reduce council tax by 2.5 per cent for 2012/13, then the use of the enabling fund would increase by £0.921 million over this period.

Financial Implications

55. These are included within the body of the report.

Legal Implications

56. There are no legal implications arising directly from this report.

Conclusion

57. This report brings together all known, relevant income and expenditure and funding information. This should aid members in understanding the major issues to be faced in setting the 2012/13 budget and allow them to consider and challenge that information before council sets its 2012/13 revenue and capital budget in February 2012.

Background Papers

Appendices

- Appendix A – revenue budget summary and budget target
- Appendix B – essential growth
- Appendix C – base budget savings
- Appendix D – revenue growth bids
- Appendix E – capital programme to 31 March 2017
- Appendix F – capital growth bids
- Appendix G – medium term financial plan

Other background papers

- Medium term financial strategy 2012/13-2016/17 – cabinet 8 December 2011
- Budget monitoring: September 2011 – cabinet 8 December 2011
- Universal credit : welfare that works (white paper) – Nov 2010 department for works and pensions
- Welfare reform bill 2011 (green paper) – February 2011 – department for works and pensions