REVENUE BUDGET 2005/06

PROGRAMME AREA RESPONSIBILITY: CORPORATE STRATEGY AND FINANCE

CABINET **24TH FEBRUARY, 2005**

Wards Affected

County-wide.

Purpose

To formulate Cabinet's recommendations to Council on the budget for 2005/06 and the associated level of Council Tax.

Key Decision

This is not a key decision. The final decision will not be taken by Cabinet but by Council at its meeting on 11th March, 2005.

Recommendation

THAT Revenue Budget proposals for 2005/06 be finalised and decisions taken on the consequent level of Council Tax for recommendation to Council.

Reasons

To agree a recommendation to Council.

Considerations

1. As its meeting on 27th January, 2005, Cabinet considered the recommendations of the Budget Panel regarding the parameters for preparation of the Revenue Budget for 2005.

2. The following paragraphs detail the information reflected in the report considered by Strategic Monitoring Committee as a basis for commenting on the budget proposals prior to a final recommendation from Cabinet to Council. The recommendations of Strategic Monitoring Committee are contained in paragraph 42.

Aligning the Medium Term Financial Plan to the Corporate Plan

3. The Council has recognised the importance of forward planning and has adopted key principles, to be reflected in budget considerations, within a Medium Term Financial Framework. Building on this approach, further work has been undertaken to develop a Medium Term Financial Plan for the period 2005/06 to 2007/08.

4. Cabinet recently agreed the Council's Draft Corporate Plan ('the Plan') for the period 2005-08. The Plan clearly sets out the Council's priorities and its direction of travel over the next three years. The Medium Term Financial Plan (MTFP) performs a vital

role in resourcing the Corporate Plan and, in particular identifies unavoidable spending pressures and the potential impact on council tax.

5. The savings figure in future years within the MTFP is based upon limiting council tax rises to broadly Government guidelines and provides a guide to the level of resources the Council has available to deliver its priorities within the Plan. There are a number of important factors to be highlighted. There is highly unlikely to be any significant headroom in the budget over the period of the MTFP given:

   - the restrictions in raising revenue locally through capping, particularly in 2005/06.

   - the requirement to identify cash efficiency savings following the Gershon Review.

   - the ongoing pressures in the funding of care for older people and waste disposal and, the continued support for Education in line with Government targets.

6. It is imperative, therefore, for the corporate savings initiative to continue through the Service Improvement Programme (SIP); corporate procurement and reducing base budgets in line with the priorities set out in the Corporate Plan. Appendix 1 details the budget reductions agreed by Cabinet at its meeting on 27th January, 2005.

7. The constraints within the MTFP demonstrate the need for flexibility in how the priorities within the Plan are funded. Three specific ways of doing this are;

   - the LPSA Performance Reward Grant will be received over the next two years and this is shown as funding improvement in Herefordshire Partnership priority areas.

   - the use of capital investment through both prudential and supported borrowing and this needs to be reflected in the capital strategy.

   - the prudent use of reserves and the flexibility accorded by the one-off changes in the current year's settlement to manage base revenue budget fluctuations over the medium term.

8. A number of priorities emerged from last year's budget considerations with a number of principles being established in setting the current year's revenue budget and the MTFP. These are as follows:

   (a) The underlying principle of the medium-term financial strategy is that the Council would intend to maintain the real purchasing power of current revenue budgets throughout the life of the plan period.

   (b) An acceptance that the Education budget will largely be driven by a national agenda which has seen investment in Education above the level of inflation throughout the life of this Council. The emphasis within that investment is on passporting cash to schools. The Council wish to support that approach whilst recognising that that does create difficulties for funding central support for schools, particularly in a Council with Herefordshire's characteristics.

   (c) There will be a need to continue to strengthen the Social Care budget through the medium-term financial plan period if the Council is to maintain improvement in this key area of its performance. This is particularly true in the area of care for older people where the Council spends significantly below its FSS.

(d) The Council has been postponing investment in Information and Communications Technology (ICT), partly because of its poor and inconsistent inheritance but also because of the difficulty of making judicious investment in those areas based on the occupation of existing accommodation. Investment cannot however be further postponed without the Council risking failure in the way it works and delivers services to the public.

(e) The Council needs to address its performance in relation to highways, transport, planning and waste. This will require prudent investment and the generation of that investment may require the Council to support significant changes in the pattern of provision.

(f) There is a need to continue to resource activity, which is of direct benefit to the community. Past inspections have led to criticism of levels of investment in adult learning and libraries. The Council needs to maintain resources for these services if it is to continue to offer them. If it is unable to maintain those minimum levels of service then it needs to consider in some cases whether to continue to maintain the services at all in some areas.

(g) The Council needs to continue to strive for efficiency. It would be foolish to pretend with an organisation of the size of the Council, delivering the range and breadth of services that it does, always maintains 100% efficiency. There is however a recognition that the amount which can be driven out by traditional approaches to improving efficiency are unlikely to be sufficiently significant to support the Council's medium-term financial plan. Cabinet has therefore agreed to look at two specific projects as an alternative to traditional approaches to economies and efficiencies. These approaches are now embodied in the work through the Service Improvement Programme and Procurement initiatives. That is not to say, however, that the traditional approaches would not continue.

The Service Improvement Programme (SIP) - this programme is intended to take a fundamental look at the way in which the Council operates. It will seek to address the prospects for savings by entirely changing operational process. It is believed that there are significant opportunities for efficiency savings. Cabinet has agreed in principle to pursuing this approach, ensuring that savings generated are freed to support the Council's MTFP rather than individual Directorate and Departmental activity.

(h) Accommodation - the Council's current occupation of accommodation is inefficient both in terms of the actual occupation of space but also in terms of maintenance and loss of staff time. Again Cabinet has approved in principle a process for managing the accommodation requirements of the Council in a way that will be at least cost neutral and hopefully over the planned period will make a modest revenue return for reinvestment.

(i) In addition, Cabinet considered the extent it wishes to resource any additional borrowing required as a consequence of the Prudential Guidelines. The MTFP reflects a provisional spend of £5,000,000 per annum. The position will be reviewed annually.

9. The 2004/05 Revenue Budget substantially reflected these principles despite capping. In the light of the funding constraints now faced, however, the above principles have been revisited in Budget Panels over the last two months with a realisation that levels of revenue investment anticipated (i.e. £7,000,000 in total less £1,800,000 invested in 2004/05) may not be able to be maintained in all areas. The following paragraphs highlight the key issues for Cabinet's consideration.

Aligning the Medium Term Financial Process to Budget Policy

10. In determining its budget policy, the Council will need to take into account immediate factors outside the MTFP. These include:

(a) the need to protect the Council's financial reputation, managing and highlighting potential risks to the medium-term financial strategy both in terms of the forthcoming annual budget but also into future years.

(b) continuing to learn from the monitoring of the current year's financial performance translating that practical experience into amendments to the budget for the forthcoming year. This requires an examination of both overspends and underspends although clearly overspends represent a greater risk.

(c) assessing the Government's financial settlement for the forthcoming year but also seeking to anticipate trends over the medium-term financial plan period.

(d) the level of the Council's general reserves and balances.

National Outlook

11. Prior to considering local priorities, as reflected in the Corporate Plan and associated MTFP, it is important to give consideration to the national outlook. The CSR 2004 sets out the Government's resource forecasts for local government for the three-year period 2005/06 to 2007/08. A detailed report has been considered by Cabinet but the following aspects are worth reiterating:

- Continued direction of resources towards Education and Social Care.
- Expectation of cost effectiveness savings to redirect to other service pressures (Gershon).
- Real terms reduction in Highways funding.
- Possible three-year settlements from 2006/07.
- Direct funding of schools.
- Transfer of Preserved Rights Funding Social Care to Review to mainstream FSS. (This transfer into the national funding stream is likely to result in a significant loss of revenue to the Council).
- The Balance of Funding Review led by Sir Michael Lyons, is due to report in December 2005 although it is too early to speculate on changes to the way local authorities are funded.

A summary of the Revenue Support Grant Settlement for 2005/06 is contained in Appendix 2.

Status and Risks

12. Clearly the need to avoid capping is critical in the determination of the level of council tax for 2005/06 and predictably also in future years. However, it is also vital that the Council has regard to the risks faced, both in terms of impact on service delivery and its status and reputation, in determining its MTFP. The following paragraphs highlight the major issues to be considered.

13. The Council has maintained its steady improvement with regard to the Audit Commission's Corporate Performance Assessment (CPA) and the recent CPA announcement sees the Council consolidate its position as a "Good" authority. Based on its current plans, Herefordshire was judged to be well placed to continue to improve the services it provides to local people. The Council has made progress on its service score for Environment but fallen back in its score for Education and Social Care (Children and Young People). The Council currently enjoys the maximum score for the "Use of Resources" and for this to continue, particularly having regard to the new CPA methodology for 2005 onwards, resources will need to continue to be directed in support of the Council's priorities

14. The CPA methodology is changing from 2005 onwards and, whilst still subject to consultation, is almost certain to involve the attainment of higher standards to maintain the Council's current classification. The Auditor's judgement, as currently proposed, will offer stronger judgements on financial planning and management, internal controls and financial standing. The mechanisms the Council has used to consult on and determine the level of resources will also be considered. The current development of the Corporate Plan and associated MTFP will be critical factors in the CPA and the Council will, therefore, need to ensure that resources continue to be directed accordingly.

15. The Council does, however, face significant risks in the following areas over the medium term.

    (a) The Social Care budget, which without ongoing investment would place the Council at risk with increased expectation, increasing number of clients and increased exposure to challenge. Continuing to press for the adoption of the 2001 census data is an important element of mitigating that challenge.

    (b) The difficulty of estimating the escalating costs of waste disposal and collection. There are a number of actions such as the need to re-negotiate the Waste Disposal PFI contract and the pressure of ever-increasing volumes of waste, coupled with the annual increases in landfill tax. There is also the cost of recycling, particularly in a scattered rural community. The standstill budget reflects the costs associated with anticipated increases in waste volumes and a provisional allowance for increased costs.

    (c) There is a need to address issues of levels of performance within Social Care (Children and Young People) which contribute to the annual star rating. This will now be reflected in the Joint Area Review of Children's Services.

    (d) In relation to other service areas, national targets and standards, which are subject increasingly to a variety of inspection regimes, do have to be met, both in the short and medium-term. They require either a realistic budget provision or for the Council to formulate a strategy for dealing with the non-achievement of those targets.

(e) Regarding the late additional funding provided in this year's settlement, it is asserted that it is highly unlikely that they will be made available next year. If not, that would place a further significant pressure on council tax in 2006/2007 and beyond.

(f) The Council is embarking on a major budget reduction exercise including SIP and Procurement savings. Significant reductions in budgets reduces the capacity to manage unforeseen budget pressures in year.

(g) Lack of affordable housing is impacting on spending on homelessness and may continue to put pressure on limited resources.

(h) Revenue Support Grant Clawback - the issuing of annual amending reports by the Office of the Deputy Prime Minister (ODPM) creates the potential for retrospective clawback of RSG as a consequence of changes to other authorities' data.

(i) The markets supplying residential care and public transport increasingly require increases in charges/subsidy beyond inflation or services are withdrawn.

(j) Significant reductions in the Supporting People Grant are anticipated over the period of the Medium Term Financial Plan.

16. As previously reported Section 25 of the Local Government Act 2003 requires the County Treasurer to report to the Council when it is determining the budget and council tax each year. The County Treasurer is required to give professional advice on those two elements which are inter-dependent and must be considered together. Decisions on the appropriate level of reserves must be considered in the context of risk and uncertainty, with decisions ultimately guided by advice based on an assessment of all the circumstances considered likely to affect the Council. Paragraphs 17 and 18 below reflect this requirement.

17. The County Treasurer, in considering the robustness of the estimates reflected in the budget and the adequacy of general reserves, has taken into account the following factors:

- **Realism of budget provision for:**
    - Pay awards and price increases.
    - Income, particularly that of a volatile nature.
    - Demand led services, most notably but not exclusively within Social Care and Waste Management.
- **Financial management arrangements currently in place including:**
    - Revenue and Capital monitoring and reporting procedures.
    - Treasury Management best practice.
    - Income collection and debt management procedures.

- Specific provisions and estimated reserves.
- Financial control procedures and internal audit reviews.
- Risk management and contingency planning procedures.

- **External influences**
  - Potential claims against the Council.
  - Changes to Revenue Support Grant funding.
  - Economic considerations.
  - Major unforeseen events or emergencies.

18. Having regard to the foregoing paragraphs, the County Treasurer is satisfied that the budgets proposed are realistic and the level of reserves are adequate having due regard to the proposed application of reserves reflected in paragraphs 19-28 below.

The Current Year's Budget and Accumulated Reserves and Balances.

19. A key factor linking the Council's budget and risk is the level of the Council's general reserves. An estimate of the position on reserves as anticipated at 31st March, 2005 is set out in Appendix 3.

20. The main features arising from this year's revenue budget which are relevant both in terms of the MTFP and the 2005/06 Budget specifically are:

- Demographic demand for older people's services.
- Waste Management – increasing costs and volumes.
- Reducing income – industrial estates and commercial property.
- Pressures on the homelessness budget.
- ICT Investment
- Grounds maintenance – adopted land etc.

21. The estimated level of general reserves at 31st March, 2005 is £5,000,000, i.e. £2,000,000 in excess of the minimum level of £3,000,000 approved by Council. Whilst the position will need to be reassessed on the basis of any further emerging issues and the Council's final budget proposals, the County Treasurer advises that a figure of £3,000,000 represents a valid and prudent reserve to maintain. A sum of £2,000,000 is, therefore, available on a one-off basis to support the Council's overall budgetary position. Once again, previous advice is reiterated that such a sum should not be used in support of ongoing revenue expenditure, not least having regard to the impact on future years' council tax rises.

22. In addition to the sums represented above, it is forecast that the Council will retain some £1,100,000 as a consequence of underspendings resulting from delays in implementing revised Waste Disposal PFI contractual arrangements come the end of the financial year. Current indications from negotiations point to significant increases in costs, at least over the next few years, which although consistent with projections

reflected in the MTFP would adversely impact on council tax, potentially by up to 1.5% - 2% from 2006/07 onwards. It is, therefore, recommended that the accumulated underspend is utilised to even out the call on the budget for the three-year period 2005/06 to 2007/08.

23. The overspending predicted for Social Care and Property Services are two areas which give rise to some concern despite ongoing efforts to contain expenditure within budgetary limits.

24. With regard to Social Care the significant efforts made in 2003/04, which saw the overspend reduce to £253,000 have been confounded by emerging pressures during the current year. It seems likely that, despite the rigorous management action applied to mitigate the position, an overspend in excess of £750,000 will result.

25. The position regarding Property Services has developed over the last few years as rent reviews and other factors has seen income levels fall. Additional resources of £197,000 provided as part of the 2004/05 budget has stabilised the position but an accumulated deficit come the year end of some £450,000 is anticipated. The Director of Environment had proposed reducing property maintenance by £200,000 a year as a means of addressing the position over the medium term.

26. Managing down these overspends against the backdrop of tight budgetary constraints over the period of the MTFP presents a significant challenge. Cabinet has therefore supported the proposition that, given the relatively healthy position reported, general reserves are utilised to reduce the overspend to be carried forward at least in part. Clearly such an approach must be viewed as exceptional given the Council's current policy of carrying forward both over and underspending as detailed in financial regulations. The position will be reviewed in the light of the final outturn for Services at the end of the financial year.

27. A further issue requiring consideration in the context of the Council's available reserves is the implementation of the Children Act 2004. The appointment of an interim Director of Children's Services paves the way for the realignment of service provision within the Social Care and Education directorates. The process will require dedicated resources additional to those currently available, to develop a clear rationale for likely change and to implement new systems, procedures and staffing structures. The Director is currently preparing a report for Cabinet consideration and at this stage additional one-off costs in the order of £250,000 are anticipated over the next two years. Cabinet has also supported the proposal for this one-off cost to be met from reserves.

28. Finally, with the pressures of job evaluation and the need for Human Resources support for major change programmes, there is the opportunity to provide temporary financial support for the Human Resources Division prior to Cabinet considering final proposals for the structuring of that Division.

Standstill Budget

29. A key component of the Council's budgetary process in recent years, endorsed by Council last year in adopting the MTFP, has been the maintenance of the real terms purchasing power of current revenue budgets. In essence, this is the impact of inflation for pay and prices on current budgets over the life of the planned period.

30. The standstill budget takes account of this anticipated inflation together with unavoidable commitments, either known or anticipated, of a corporate i.e. council-wide nature. Account is also taken of changes to the budget required as

a result of the transfer of funding between mainstream RSG funding and Specific Grants (e.g. Preserved Rights Grant). The position reached is the total cost of providing current levels of service before taking into account service pressures, budget reductions or any other policy decisions. Standstill budgets for 2005/06 to 2007/08 are reflected in Appendix 4.

31. Government funding through the Revenue Support Grant (RSG) mechanism is then taken into account to arrive at the council tax required to meet the approved level of spending.

32. The net standstill budget for 2005/06 is £184,697,000 which, after RSG and Collection Fund surplus of £117,942,000, leaves a sum of £66,755,000 to be funded by council tax. The figure is before taking into account development pressures, e.g. Social Care and ICT and before any budget reductions and generates an increase in council tax of 4.0%. The increase now reflects the small change in RSG provided in the final settlement.

Council Tax Capping 2005/06 and Beyond.

33. The prospect of Government using their capping powers remains a very real possibility for authorities deemed to have 'excessive' rises in Council Tax. The following paragraphs highlight key elements emerging from the Revenue Support Grant Settlement particularly the potential impact in 2006/07.

34. As detailed earlier in this report, and reported to Cabinet on 16th December, 2004, the provisional local government finance settlement issued by the Office of the Deputy Prime Minister on 2nd December, 2004 was significantly better than that which could have been predicted from the CSR 2004 announcement in July. Those improvements, followed intensive negotiation between the Local Government Association (LGA) and Government over the intervening period. Whilst that relief is welcomed, as reported to Cabinet on 16th December, 2004, on the face of the announcement, there was the clearest possible indication that £3 million of the additional monies made available in support of the current year's settlement will not be repeated in 2006/07. There has been further opportunity to examine the detail and it is clear that applies both to the sum of £1.5 million addition made available through the late changes to the settlement and also to the proposal to postpone the technical adjustment in relation to the preserved rights expenditure (Social Care) which is currently funded by specific grants where the intention remains to transfer this into mainstream FSS funding, which may disadvantage Herefordshire to the tune of £0.8 million. There is, therefore, a total potential impact on the 2006/07 budget of £2.3 million. The final settlement, announced on the 27th January, 2005, showed a marginal improvement on the provisional settlement.

35. There remains the possibility that as in the current year, there will be adjustments made to the underlying CSR 2004 announcement in relation to 2006/07 but the current very clear message is that similar adjustments next year are not in contemplation.

36. The other important factor to which to draw attention and which is easily overlooked as part of the Government's announcement, is that part of the additional monies made available is expected to be applied to drive down still further the levels of council tax which will need to be levied. The average national figure to which the Government is making reference in its announcements is 3.7% but employing exactly the same method of calculation for Herefordshire's own position then the predicted council tax increase in Herefordshire would be some 4.8%. Before the council tax is set in March, it will be important to look at the council tax rises being generated within

the region, to look at those being generated by similar County authorities and to look at those being generated by similar Unitary authorities. Early indications are that council tax increases are more likely to be in 4% - 4.5% range and it clearly is a priority for the Council to avoid any risk of "capping" in the forthcoming financial year. At the same time, it is important particularly given the one off nature of much of the additional assistance in the current financial year, that the Council maintains the highest possible base because that will give the maximum flexibility in dealing with the challenges which are clearly set out in the supporting Appendix 4.

Budget Recommendations to Council

37. Cabinet has established the following key principles to be applied in the setting of the Budget for 2005/06 and the associated level of Council Tax.

- The very real possibility that RSG will be significantly reduced in 2006/07.
- The consequential need to deliver budget reductions as reflected in Appendix 1.
- The need to provide additional resources for Older People Services and ICT in the total sum of £1m.
- The need to secure Service Improvement Programme and Procurement Savings.
- The need to resource Invest to Save initiatives, including accommodation rationalisation, the service improvement programme and other measures which will generate economies to assist in minimising the impact of grant reduction in 2006/07 and beyond.
- An increase in Council Tax of between 4% and 4½%.

38. The position may be summarised as follows on the basis of a 4% increase in Council Tax.

	£000	**£000**
Standstill budget reflected in Appendix 4.		184,697
Older Peoples Services and ICT		1,000
Budget Reductions	(3,056)	
Invest to Save provision	2,048	(1,008)
Total budget requirement		184,689

39. Supporting schedules for each programme area are attached at Appendix 5.

40. The impact of the Children Act and the consequent appointment of the Director of Children's Services requires a major restructuring of both the Education and Social Care budgets, as referred to in paragraph 27. A comprehensive review of the budget allocation between Adult and Children's Services will also be required. It is therefore inappropriate, at this stage, to make firm final decisions on the allocation of the

additional £1,000,000 between Social Care and ICT services. A further report to Cabinet in the spring will provide the basis for the allocation of the additional budget provision.

41. Similarly, the allocation of the Invest to Save provision to priority initiatives will also require further consideration by Cabinet as proposals are put forward. Reports will also reflect progress on the attainment of Service Improvement Programme and Procurement savings which will add to the Invest to Save provision.

Recommendations of Strategic Monitoring Committee

42. Cabinet will wish to consider the views of the Strategic Monitoring Committee following its meeting on 8th February, 2005. The Committee resolved as follows

a) the approach to preparing the 2005/06 revenue budget, as reflected in the recommendations of the Budget Panel as endorsed by Cabinet, be supported in principle, subject to the caveat that the assumptions made about the savings which it was expected could be achieved by efficiencies and other means needed to be viewed with caution; and

b) whilst recognising the Cabinet and Council needed to consider the budget in strategic terms it was important that all Members were provided with the detail of the proposed budget reductions summarised in Appendix 1 to the Cabinet report. (This information is now provided as part of an expanded Appendix 1).

Consultation Results

43. The Council has again consulted widely on the budget utilising a range of approaches from public meetings to a representative survey of households across the County. Cabinet considered the results at its meeting on 27th January, 2005 and whilst recognising the difficulties inherent in public consultation, particularly when considering a detailed package of options, felt that the results were helpful in informing the Council's decisions over the period of the Medium Term Financial Plan.

44. The Research for Today survey also indicates that the majority of adults would be likely to favour a package which combines a relatively modest increase in Council Tax with, if necessary, targeted service reductions of up to £3,000,000.

Risk Management

Due consideration of the budget is required to ensure that financial reserves are directed in accordance with the Council's policy objectives. Paragraphs 12-28 of the report detail strategic risk issues.

Consultees

Budget Panel, Strategic Monitoring Committee, Local Area Forums and the general public.

Background Papers

None identified.