Report to Cabinet – 17 September 2007

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AUTUMN BUDGET STATEMENT

Summary

This paper sets out the context, at both the national and local level, within which the County Council's medium term financial plan will be framed over the next three years.

There are three critical issues facing local government at the moment. The first issue is about the totality of resources that will be available at a national level for our services which will flow from the national Comprehensive Spending Review 2007 due in October. The second is about how those resources will be distributed to authorities through formula grant and specific grants, with the former having particular implications for authorities such as Kent who are currently floor funded. The government is currently consulting on changes to the formula grant and the deadline for response, to which the County Council will of course respond, is 10 October. The third is how we balance increasing demands on our services due to demographic and wider socio-economic change, government imposition of new burdens, climate and environmental change, rising customer service expectations and indeed our own aspirations for continued innovation and improvement in services at a time of nationally and locally constrained resources.

Recommendations

To note:-

1. National Context:

- that the outcome of the delayed Comprehensive Spending Review 2007 will inform the overall financial parameters within which we will be able to work
- that the subsequent local government finance settlement, which will be dependent upon CSR 07, will be the first full three year settlement for local government covering the period 2008-11

2. National Resources Position:

- key driver of resources for local government in total will be CSR 07
- pre-announcements for many central government departments include a raft of minus 5% in real terms per annum budget reductions - the funding position will therefore be significantly constrained
- awaiting spending announcements on the NHS, defence and local government amongst others
- Institute for Fiscal Studies suggests there may be a little as 0.4% real terms spending available for all remaining services not yet announced, after allowing for expected increases for the NHS

- currently there is a major consultation on reforms to the local government finance formula which will set the formula for the next three years
- outcome of local government finance settlement remains extremely uncertain both at national level and individual authority level

3. Kent – Local Resource Allocation

a) the items on which KCC and partners are most concerned are:

- the local impact of the Comprehensive Spending Review 2007
- the overall resources available to fund service pressures and inflation
- regional disparities, in particular flowing from the Barnett formula and other regional comparisons
- the funding of the Growth Agenda
- the operation of the main funding formula and its inbuilt deficiencies which fail to adequately reflect Kent's unique features
- the operation of Dedicated Schools Grant and its inbuilt deficiencies in terms of resource allocation and the total quantum of funding
- the burdens imposed upon us by government without adequate recompense in terms of additional funding
- a continued failure by government to assure us that it will fully reimburse asylum costs

b) KCC has been and will continue to lobby and influence the CSR as it progresses.

c) KCC has developed and strengthened its policy led budgeting yet further to ensure that it optimises the allocation of constrained resources to meet local priorities

d) the financial planning risks for KCC which are set out in paragraph 98 onwards of this report

e) the proposed Medium Term Planning key milestone dates set out in Appendix 1.

Background Documents: None

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AUTUMN BUDGET STATEMENT

INTRODUCTION

1. This report is a key stage in medium term financial planning. It provides an opportunity to review both the national and local contextual issues that will shape our forward thinking for the next three years. It also gives direction to the necessary actions required to deliver the Council's policies and priorities and sets out the financial framework for the budget and medium term financial plan, which will be presented for formal agreement by Council next February.

2. The report is in two parts. Part 1 sets out the national context for the Council's financial plan over the next three years. In particular it looks at what resources will be available to local government from the national perspective. Part 2 is about delivering the medium term plan in KCC within the context of the likely distribution of the total national resource to Kent over the medium term.

PART 1: NATIONAL FINANCIAL CONTEXT: RESOURCES

3. Budget planning takes place within the context of the national economic and public expenditure plans. This part of the report discusses the broad national assumptions within which the budget and medium term plan will be framed.

The Economy and Public Expenditure

4. The Budget 2007, announced on 21 March, is the most recently published document setting out the government's view of the national economic situation and the public finances. Featured, were the plans to remove the 10 pence starting rate of tax, and to cut the basic rate of income tax from 22 pence to 20 pence from April 2008. The Chancellor reaffirmed that inflation is expected to stay at a 2.0% target rate, with CPI returning to target in the second half of 2007. The economy is expected to grow from 2.75% to 3.25% cent during the year, and from 2.5% to 3.0% in 2008 and 2009. The Chancellor will be presenting his pre-budget report in October 2007, which will provide updated forecasts of the public finances and will set the scene for the 2008 Budget.

5. The Bank of England's Monetary Policy Committee increased base interest rates on 5 July 2007 from 5.5% to 5.75%, the sixth rate rise since last August. Interest rates are now at their highest since March 2001. These decisions are reflective of continuing inflationary pressure in the UK economy (see below).

Inflation in the Public Sector

6. Inflation is currently running at 1.9% (CPI July 2007). Whilst the trend in this figure is now downwards, primarily due to falling gas and electricity prices, it has previously remained well above the government's target rate. The rate has not previously been at or below the target rate of 2.0% since April 2006, and rose to a high of 3.1% in March 2007. In contrast RPI, the inflation measure which is used for benefits indexation, is currently running at 3.8% (July 2007). There is a particular upwards pressure on the RPI from mortgage interest payments (excluded in CPI) which have been rising as the base rate has risen. The interaction of higher interest rates and lower CPI has made trend patterns harder to establish for RPI but, until this month, the rate has been consistently above 4% since last December.

7. In the Chancellor of the Exchequer's Budget 2007 Statement, it was commented that whilst other economies had seen an inflation increase of over 3.0% at some points, because of rising oil and commodity prices, Britain had never gone over this mark. This is now not the case, the position being breached in March 2007 although the CPI is now beginning to fall.

8. Neither CPI or RPI may be the best rates to use when considering public sector inflation. One of the biggest difficulties in dealing with this area is to find any robust consistent method of measuring public sector inflation. The current methodology is derived from public sector outputs and has been revised many times by the Office for National statistics (ONS). The Chief Secretary to the Treasury has agreed in principle to develop a measure of public sector inflation but progress on its implementation has been slow and there has to be concern that part of the reason for delay is that if there is a measure available which demonstrably shows funding increases at a rate less than inflation that government will feel under pressure, and rightly so, to increase its funding for local government.

9. The Adam Smith Institute has previously set out an argument that shows that public sector inflation (PSI) has run at almost 5% per year since 1997. Our estimates, based on current budget data continue to be consistent with a local price inflation rate in excess of 5%.

Government's Current Spending Plans

10. Spending Review 2004, published in July 2004, set out the government's spending plans for the period 2005-06 to 2007-08. This remains the prime source of funding information for local government as a result of the delayed announcement of the Comprehensive Spending Review 2007. Until CSR 07 is announced we simply have no published macro economic intelligence to base our spending and financing assumptions on.

11. The Budget 2007 highlighted the following:
- public spending (combined revenue and capital) is to increase by an average of 2.0% per year in real terms.
- landfill tax to increase to £32 per tonne in 2007.
- spending on education is to increase by 2.5% in real terms.
- it is not clear how councils will pay for the increasing costs of the aging population, and the burdens in later years.

Comprehensive Spending Review 2007 (CSR07)

12. On 19 July 2005, HM Treasury announced the second Comprehensive Spending Review (the first being 1997), which will report in 2007. CSR07 will examine what the investments and reforms initiated to date have delivered and what further steps must be taken to ensure that Britain is fully equipped to meet the challenges of the decade ahead.

13. In July 2006 HM Treasury released an interim report on CSR07 called "Releasing the resources to meet the challenges ahead". This set out the key elements of a wider programme of public sector reform and for the activities to achieve better value for money and improved investment.

14. The Government will publish the second Comprehensive Spending Review, now later than anticipated, in Autumn 2007, which will set spending limits for 2008-09, 2009-10 and 2010-11.

15. It is anticipated that CSR07 will reflect the worsening of the economic situation in the country, and that increases in grant will be below that of previous spending reviews.

16. The projection of growth is expected to be 2.0% in real terms (combined for revenue and capital spending), i.e. in addition to the rate of inflation. Existing commitments for Health and Education, amongst others, will eat into this real term growth, meaning that some services will get markedly less.

17. Nine government departments have received early CSR07 settlements with Departmental Expenditure Limits (DEL) declining by 5% per year in real terms over the three years term of CSR07. The Home Office has agreed an early settlement that maintains its DEL in real terms over the CSR period.

The 'Four Block' System

18. In 2006-07, settlements began adopting a new 'four block' system for formula grant, which means that total assumed spending and formula spending shares (FSS) no longer exist.

The four blocks of the model are as follows:

i. Relative Needs Block – worked out using the Relative Needs Formulae (RNF), this is the equivalent to FSS
ii. Relative Resource Amount – takes account of different capacity to raise income for council tax (a negative amount for KCC)
iii. Central Allocation Amount – allocated on a per capita basis
iv. Floor Damping Block – to ensure that all authorities receive the minimum grant increase

19. The four block system is less transparent than the previous FSS system, and it is harder to explain to key stakeholders. This is because it is no longer possible to easily find out the total the government is prepared to support through grant and how much of this is assumed to be financed by councils' own resources (i.e. council tax).

20. Government is currently consulting on changes to the formula funding (deadline for response is 10 October 2007) and it is expected that these changes will be announced at the same time as the three year settlement in late November or early December. This adds further uncertainty to the overall funding package making it incredibly difficult to plan with certainty now. KCC will of course comment vigorously on the proposed changes to ensure the best outcome for Kent residents and argue for a fair share of the resource allocation.

Education Funding and Dedicated Schools Grant

21. The DfES (now the Department for Children, Schools and Families) launched its five-year strategy for Children and Learners in July 2004, which set out key reforms including guaranteed three-year budgets for every school from 2006, tied to the CSR cycle and geared to pupil numbers, with every school also guaranteed a minimum per pupil increase each year. The DfES introduced this funding mechanism in the form of Dedicated Schools Grant in 2006-07. Indicative funding was announced for 2006-07 and 2007-08. A consultation took place in early 2007 about potential changes to this funding system for the period 2008-11 and decisions on that were announced on 25 June 2007..

22. The recent June announcements mean that the risks that we identified with the DSG system when it was introduced will continue for the next three years. Decisions on schools budgets will still have to be taken before DCSF announce the final DSG, due to lags in the DCSF systems for processing and verifying pupil data. Local decisions therefore have to be based

on indicative allocations with a mechanism to deal with under and over allocations. This was a significant issue for us in 2006-07.

23. The recent announcements do not change the fact that the funding arrangements seem to be based on an assumption that there is a national “one size fits all” solution to the funding of schools. The new system leaves little room for changes to reflect local needs and priorities. It also assumes that at the point in time that these changes were introduced the local schools formula was “right”.

24. On top of this, subsequent DCSF announcements have led to increased spending pressures on schools and the authority. The most significant of these was in relation to the Teachers Pension Scheme. The employers’ contribution has increased from 13.5% to 14.1% from 1 January 2007. The estimated annual impact is £2.4m which had to met by schools from other savings as this was not funded within the national DSG settlement.

25. There are immense pressures from Government stated commitments and priorities. By 2008/09, there is estimated to be an excess pressure of £11m on DSG funded services and no funding headroom to pay for this. The only option to close the gap other than cutting services would be to top up funding from council tax. But with funding pressures of our own it is wholly unacceptable to expect local taxpayers to top up a supposedly nationally funded schools service.

26. The overall impact of these changes has meant that the supposed headroom that the authority has (which is the difference between overall DSG funding increases and the amounts that have to be passported to schools and schools spending under the funding guarantee) may well become negative.

27. The decisions about the future funding framework that were announced in June 2007 include some significant longer term changes in respect of funding for schools and early years, Subsequent announcements have made it clear that by 2010 all funding for 16-19 year old students in schools and FE Colleges will be removed from the LSC and returned to local authorities through the DSG. By 2010-11 we have to have established a single local formula for all early years funding (maintained and PVI). By 2011-12 there should have been a wider review of the national methodology for DSG distribution to local authorities , from which a single formula for all should be announced. This could adversely affect Kent.

28. For KCC, there is a further particular concern in relation to the funding of those parts of the DSG that cover Early Years and non-delegated items such as spending on the , Education Welfare Officers (EWOs), Attendance & Behaviour Services, Pupil Referral Units etc. As a first call the DSG must fund the nationally set minimum per pupil increases in schools (the minimum funding guarantee), which means that the resources available in the DSG for the other services such as these may be squeezed to unacceptable levels. This is particularly an issue in terms of the early years funding for the PVI sectors where the DCSF announcements have built up a degree of expectation about improved funding despite the fact that there are no indications about any extra money being made available in the DSG. More detail on this is still emerging but we are unlikely to have any detailed information until CSR07 is announced in the late autumn.

29. There are continuing worrying issues in relation to new responsibilities and pressures for schools. The June announcements were clear that the DSG will include “substantial assumptions about the (cash) efficiencies schools will be expected to achieve over the next three years“ Schools are already having to make efficiency savings in order to balance their budgets because of the impact of falling rolls so this is effectively a “double hit” on them, exacerbated by the fact that local authorities will be required to claw back 5% of each schools reserves. It is crucial that the government correctly estimates and funds the costs

of pressures on the DSG. Alongside this there is the concern that there are no national mechanisms in place to reflect significant local pressures on schools – such as the big price increases schools face when long-tem contracts for services such as energy, catering and cleaning come up for renewal – apart from squeezing that element of the DSG that funds other local authority services for schools and pupils. It was this failure to properly assess the costs that led to the national funding "crisis" in 2003.

Local Government White Paper 2006: Strong and Prosperous Communities

30. The Local Government White Paper was published on 26th October 2006. The paper indicates the next stages of public reform, and aims to 'enable effective local services and create better places, through new relationships and better governance' (Strong and Prosperous Communities, January 2007).

31. The paper encapsulates two big themes, both focused on empowerment. First of all, it proposes devolving more power to the local community, allowing more choice and greater opportunity for locals to have a say in how their local services are run. In order to achieve this, there needs to be a greater devolution of power from Whitehall to Town/County halls, to allow local authorities to be at the 'heart of sustainable communities'. The paper realises the importance of local knowledge, and the need for local authorities to be leaders and place-shapers. It acknowledges that communities must be at the centre of reform.

32. The Government has implemented a plan to execute the key proposals from Volume One of the White Paper. The plan has been informed by the Local Government Association (LGA), the Audit Commission and the Improvement and Development Agency (IDeA), and will be updated on the Communities website every six months and/or when major milestones have been met so as to keep it relevant and up to date. There are five main workstreams:

- Workstream 1 Local Government and Public Involvement in Health Bill
- Workstream 2 Performance
- Workstream 3 Governance and empowerment
- Workstream 4 Cities and regions
- Workstream 5 Community cohesion

Lyons Inquiry into Local Government

33. The Lyons Inquiry final report was published on the 27 March 2007 after much delay. The report was an independent inquiry into the role, function and funding of local government.

34. In the months preceding the Lyons Inquiry, staff held consultative events across the country for local people and business representatives. The Inquiry was also represented at various conferences on public and voluntary sector issues.

35. Sir Michael Lyons asserted the following:

- That local government is pivotal to the survival of communities, by offering greater choice and flexibility.
- That there should be a new partnership between central and local government. There needs to be devolution of decision making powers from central to local government, and at the same time, the latter should engage more effectively with its local people.
- Council tax is not 'broken', but is seen as unfair.

36. Recommendations included:

- ring fenced grants should be reduced, thereby decreasing control from central government. Other ways of improving flexibility include ending the capping of Council tax; levying a supplementary business rate; and a new power to charge for domestic waste to help manage pressures on council tax.
- council tax benefit should be renamed a rebate, so as to break down barriers of those who feel a stigma about collecting benefit (there is currently £1.8billion of unclaimed council tax benefit). The saving limit of pensioners should also be raised to £50,000. Ultimately, council tax should be updated, possibly by adding 2 new bands (one higher and one lower), and houses should be revaluated more frequently.
- there should be a more independent public voice informing the public and parliament about the contribution of national taxation, thereby improving the transparency of the funding system.
- local prosperity and growth should have further incentives, initially through the reform of the Local Authority Business Growth Incentive Scheme (LABGI).
- in the medium term, it should be considered whether to proportion a fixed amount of income tax to local authorities. There should also be more incentives within the grant scheme.
- consider the introduction of a tourist level in some areas.
- in the long term, it might be beneficial to consider radical changes such as a local income tax, but much more public support and understanding is necessary than currently exists.

37. The recommendations on both local government finance and the future role and responsibilities of councils could take many years to implement.

National Spending Pressures

38. The Chancellor of the Exchequer has placed affordable housing as one of his main priorities, asserting that 3 million new homes will be built by 2020 – an increase of 250,000 from the previous plan.

39. Long term challenges as likely to be identified in the CSR07 include the global climate, waste, increases in the old age dependency ratio.

40. A draft Climate Bill was published in March 2007 to set targets for reducing carbon emissions. An Education Bill will raise the compulsory age of school leavers from 16 to 18.

41. The three biggest areas of funding strain are health, housing and education.

Local Government Pension Scheme

42. The regulatory framework for the new LGPS scheme will come into effect from 1st April 2008.

43. To address the general trend of increased life expectancy (and therefore pensioners claiming their pension for longer), the new scheme aims to make the LGPS more affordable and sustainable. Removing the 85 year rule, those who retire under 65 will receive slightly less, where those who retire later receive the full benefits. It is however, payable for a longer period for all involved continuing the overall strain on the pension fund.

44. On average, employers pay in twice as much as employees do- meaning this will also be payable for longer. The Government wanted to ensure no additional costs were imposed on the taxpayer, so plans are to be in place by March 2009 to have a mechanism of sharing future costs pressures. The actuarial valuation of the new scheme will not be until 2010,

and individual fund actuaries will set new employer contribution rates to take effect on 1 April 2011.

45. In the meantime we are currently faced with the triennial revaluation of the scheme in transition as at 31 March 2007 and the results will be known in late October. On balance, though, there appears to be some additional upward pressure on employer contribution rates to come due to longevity despite good investment performance. The recent market turbulence will have no impact on this triennial valuation.

Care Matters – Time for Change White Paper

46. Building on the Green Paper, Care Matters: Children and Young people in Care, this White Paper sets out the steps the Department for Education and Skills (now the Department for Children, Schools and Families) and local delivery partners will take to improve the lives of children in care.

47. The Paper sets plans for the increased stability of care placements; ensuring children are in school and making good progress; ensuring children in care have access to leisure and recreation activities; making sure the children have a voice which is heard by councils.

48. Financial methods to take effect include the provision of £500 per year for a child in care's education and introducing a national bursary of £2,000 for all young people in care that progress to higher education. There are also to be pilot programmes placing young people up to 21 years old in foster care. The implications these will have on resources will likely require additional funding.

49. The White paper does provide additional funds to implement these changes, namely £89/£96/£107 million over the 2008-11 CSR07 period. £22.5million of this will be specifically for a dedicated change fund but it is not clear how this will actually be allocated.

50. The LGA suggest there is a lack of attention in the paper to the weak links in place between the Youth Justice system and children in care; and also the issues for asylum seeking children.

Interaction of services with the NHS

51. There is a continued grey area between the NHS and local authorities in the responsibility for provision of some aspects of health and social care. The well documented and reported upon funding crises affecting aspects of the NHS are beginning to be felt by local authorities. KCC is no exception to this pattern.

52. The LGA has published a report following a study of local authorities operating in areas where NHS trusts are in deficit. Returns were received from 55 of the 78 local authorities in those deficit areas. Of these, 67% indicated that the deficit had had an adverse effect on the authority. It demonstrates that trusts have adopted a number of cost-cutting measures that have impacted on councils, including:
- The withdrawal of funding from jointly funded projects
- A sharp increase in the referral of patients that would normally be cared for by the NHS
- Paying no more than one per cent inflation on existing joint contracts
- Closure of beds

53. Measures local authorities have adopted to cope with the cutbacks have included:
- Withdrawing services from people with lower-level care needs
- Increasing waiting times for social care assessments and services

- Outsourcing more services
- Transferring resources from other services – including leisure facilities and transport
- Using budget reserves
- Negotiating with – or taking legal action against – the NHS over the non-payment of bills

54. The Audit Commission has reviewed several aspects of the funding of the Health service, and published three reports, all of which have a bearing on this. The main themes identified were:
    - The increasing severity of the deficits, and the concomitant difficulties of recovering from these
    - The needs for appropriate skills, leadership and cultures to be developed within the NHS organisations
    - The importance of a robust financial management framework to support radical service configurations, where these are deemed to be necessary

55. The position in Kent is that the overall Health economy was in deficit in 2006-07 *(check?).* Work is underway in the current year to develop and implement turnaround plans, but the scale of the challenge should not be under-estimated. A review has been commissioned by KCC. Emerging findings for KCC include:

    - The robustness of financial management and organisational frameworks in PCTs during reorganisation
    - The level of management capability within the acute sector to deal with ongoing financial problems, particularly at East Kent Hospitals
    - How the new SHA will balance its efforts between the Kent and Surrey areas to ensure that the recovery programme in Kent does not falter, whilst accelerating the pace of recovery in Surrey and Sussex

56. The purpose of the report is to ensure that there is a robust understanding of the current position across the county, on which all further discussions and agreements can be based. At the same time, managers are working carefully to ensure that the risks and uncertainties arising from the difficult financial environment do not impact on services or service users. The budgetary risk is also being carefully monitored; and where appropriate Health decisions are being challenged. There will continue to be risk for the council's social care services all the time that the Health economy locally is so stretched. However, it is also clear that there can be no resolution to this difficulty unless the council is constructively engaged.

57. The new Health Secretary Alan Johnson has announced a review of the NHS to inquire how the service should be run over the next decade. The review is to be completed by July 2008. British Medical Association discovered in June 2007 that only a third of the public believe Labour's reforms have improved the NHS (Public Finance, July 2007). Some of the main issues for the public are access to GPs (including opening hours), unfriendly staff, and contracting infections whilst in hospital. An answer might be a new NHS Bill of Rights.

58. The Government published the Local Government and Public Health Bill on the 13 December 2006.

59. In order for local Councils to take greater share of responsibility in public health and health services, central Government is abolishing the Patient and Public Involvement Forums and the Commission for Patient and Public Involvement in Health are to be abolished. This is to take effect by 31 December 2007, and will be replaced by the Local Involvement Networks (LINKs). The prime function will be to *gather information and make the views of the public know about local health and social care services* (KCC meeting, 23 January 2007). LINKs

will apply to all councils that are responsible for Social Services. Whilst the administration will be outsourced, Dover District Council and its Primary Care Trust have agreed to be a pilot.

Differences across the UK

60. It is also perhaps worth noting and contrasting the different funding levels that exist between England, Wales, Scotland and Northern Ireland at a time when the balance of funding is being reviewed. The Barnett Formula, which was introduced in the seventies, and has not been reviewed since, results in substantially more public spending in these countries than in England. It is time that the formula was reviewed to see if it still accurately reflects relative needs.

Table 1 - Public expenditure by region/country

Country/Region	Spend £ per head of population 2006-07 plans
England	7,121
Of which South East	6,304
Scotland	8,623
Wales	8,139
Northern Ireland	9,385

(Source: HM Treasury: Public Expenditure Statistical Analysis, 2007, table 9.11)

Council Tax Increases

(a) Sustainability of Council Tax Increases

61. Council Tax has been increasing at a level significantly above inflation for a number of years.

62. The government expects council taxpayers in the South East, excluding London, to bear a much higher proportion of spending than in other regions, particularly in the North and Midlands. Table 2 shows that the proportion of spending borne by the council taxpayer is around 54% in the South East in 2007-08, but around 42% in the North East.

Table 2 – Funding, Grant and Council Tax in 2007-08

Region	Proportion of Budget Requirement met by council tax %	Grant increase %	Increase in Band D for all tiers %	Average council tax per dwelling £
Kent	**47.3**	**2.7**	**4.9**	**1,152.12**
South East	**54.3**	**3.4**	**4.4**	**1,254.84**
South West	55.7	4.3	4.5	1,157.69
Eastern	47.1	4.2	4.5	1,183.31
East Midlands	40.1	4.5	4.1	1,036.40
West Midlands	42.1	4.0	4.1	1,019.50
Yorkshire & Humber	46.0	3.6	4.2	958.86
North West	43.3	3.7	4.4	1,002.10
North East	42.5	3.5	3.8	966.94
London	42.2	3.4	3.6	1,167.34
England	45.1	3.8	4.2	1,101.19

Source: Communities 2007-08 Settlement data; CIPFA council tax statistics 2007-08

(b) Capping

63. KCC and the LGA are both opposed to capping. Ministers have reiterated that the government is prepared to use its capping powers to protect council-tax payers from excessive increases where necessary.

64. Ministers have indicated that increases in excess of 5% will be subject to scrutiny and run the risk of capping.

65. Although 35 authorities had increases that exceeded the stated 5% (in many cases because police authority precepts rose substantially in many areas) no authorities were actually capped in 2007-08.

66. However, no formal decisions have been taken at this stage on capping next year and beyond.

67. The Lyons Inquiry asserts that capping should be dropped. The government have dismissed this recommendation.

PART 2: DISTRIBUTION OF RESOURCES IN KENT

Provisional settlement 2008-09 to 2010-11

68. Due to the delayed CSR 07 announcement we have no formal basis for making any deliberations about the detail of our grant settlement from government for the next three years

69. All we know with certainty is the existing grant and the overall macro economic picture. We are therefore explicitly assuming a standstill position in grant terms for the County Council for the next three years. This also assumes floor funding protection at 0%.

Table 4 – Formula Grant for KCC as announced at 2006-07 Settlement

Formula Grant	2006-07 £m	2007-08 £m
2006-07 Settlement	226.2	
2006-07 Adjusted for specific grant and function changes	222.7	228.7 + 2.7%

70. It is unclear at present what specific grant and function changes will be reflected in the provisional and final 2008-11 settlements. Although the governments New Burdens doctrine is meant to recompense for function change at a national level it is not always clear that this is the case and furthermore distributional impacts on individual authorities at a local level can vary enormously. Where we are disadvantaged we will have no option, given the likely overall tight settlement, but to consider ceasing services where government ceases to financially support us adequately.

KCC Input to Comprehensive Spending Review 2007 (CSR07)

71. KCC has been and will continue to lobby and influence the CSR as it progresses. KCC has produced a document *Input into Comprehensive Spending Review 2007*, which provides information about the shortfall in funding that Kent suffers. This was submitted to HM Treasury on 26 May 2006.

72. We believe KCC has been under-resourced for some time and CSR07 is the appropriate juncture for the Government to take stock of resource allocation

73. In addition to this we believe that KCC does not receive the appropriate level of regional funding. Data from Public Expenditure Statistical Analysis (PESA) shows that the South East has one of the lowest regional Government spending per head of population with £6,304 per head in 2006-07, compared to £8,177 per head in North East and £8,623 in Scotland.

74. *Input into Comprehensive Spending Review 2007* makes proposals that Kent County Council urges the Government to take forward to address the potential shortfall in funding.

Local Area Agreements and Local Public Service Agreement 2

75. SR 2004 proposed the development of Local Area Agreements (LAA), a single framework operating at the local level to provide additional funding to areas. These involve government departments, local authorities and voluntary and community bodies coming together to agree where best resources might be allocated.

76. The Local Area Agreement is between Kent County Council, working with the Kent Partnership and other local partners, and the Government. The agreement covers the period 1 April 2005 to 31 March 2008 and comprises a set of 18 outcomes. These had been developed and agreed by a very wide range of partners across Kent. The indicators and targets are likely to change in the CSR07. Along with the outcomes, the other two core elements of the LAA are negotiating freedoms and flexibilities to assist delivery of the outcomes and the identification of funding streams to support delivery.

77. The Local Public Services Agreement 2 (LPSA2) has been developed alongside the LAA and all of the LPSA 2 targets contribute to the LAA. The total amount available on successful conclusion of all targets in LPSA2 is in the region of £36 million for all Kent partners and £32 million for KCC alone. We estimate KCC and its partners are likely to receive in the order of £23 million.

78. We are currently negotiating with government the second local area agreement. Government has indicated these will be delayed beyond 1 April 2008 and the implications

for wave 1 pilot authorities such as KCC whose first agreement runs out on 31 March 2008 are still being worked through.

79. We trust though that the announcements by the Local Government Minister on 3 July of a "new concordat between central and local government" and the announcements of the Chief Secretary to the Treasury on 18 July announcing a reduction in the number of PSA targets and a culture shift away from the strict target driven regime of the past decade will be reflected in the reality of a new LAA and not remain rhetoric.

The Efficiency Agenda

80. The report in July 2004 by Sir Peter Gershon on "Releasing Resources for the Frontline: Independent Review of Public Sector Efficiency" required 2.5% efficiency savings per annum for Local Government. KCC's Medium Term Plan sets out a commitment to deliver more than £86m of budget savings and income generation over the next three years. In addition we are identifying other savings where we have increased quality or quantity of services within the same budget.

81. We have consistently met and indeed exceeded the government's Gershon efficiency targets.

82. It was revealed in the Pre-Budget report 2006 that the efficiency saving will increase to 3% per annum. This might not necessarily be 3% for all services, so will schools be more than or less than the 3%? This detail is likely to be published alongside the CSR07. If it is indeed 3% across all services, then around £31m per annum will be cashable for schools and £32m per annum for non-school services - an ultimate of £63m cashable per annum. We expect this will be contained within the overall grant settlement, hence the assumed 0% per annum increase in formula grant. This efficiency target will get increasingly difficult to meet, given that in the past three years we have delivered some £90 million of efficiencies. The compounding effect of a further three years of 3% efficiency savings will be a huge challenge. An indication of the quantum of such efficiency savings, assuming a straight 3% across the board, is shown as a guide in Appendix 3.

83. Councils are required to submit Annual Efficiency Statements to the Department for Communities and Local Government setting out actions they have taken and cumulative efficiencies identified and ultimately achieved.

84. The drive for efficiencies and savings is not a new one for KCC. Savings in the published budgets of KCC amount to a cumulative £141.8 million between 2000-01 and 2006-07.

85. KCC submitted its first backward looking Annual Efficiency Statement for 2004-05 in June 2005 which set out achieved efficiencies of £21.8m. The second backward look Annual Efficiency Statement for 2005-06 set out achieved efficiencies of £21.9m. The third backward look Annual Efficiency Statement for 2006-07 set out achieved efficiencies of £17.9m. The forward looking Annual Efficiency Statement for 2007-08 sets out planned efficiencies of a further £30.7m.

86. Total efficiency savings of £90.3m have been or are planned to be achieved. Compared to the target saving of 2.5% per annum our performance represents an over achievement of some 72% against target.

Comprehensive Performance Assessment

87. On 22nd February 2007, it was announced that the KCC had achieved the highest 4 star rating for its annual CPA for the fifth year running, and that its direction of travel is 'improving strongly'. Many of the services have risen to new heights, for example the Culture score has gone from a rating of 2 to 4.

88. Only one other county council was rated four star, judged to be 'improving strongly', and awarded the highest mark for use of resources. Of the two county councils we had the lowest Band D Council Tax.

89. At the end of January 2008 a full corporate assessment inspection will take place, combined with an assessment on services for children and young people. This will be the most significant review the council has undergone since 2002. The Comprehensive Area Assessment will take place in 2009.

Growth Agenda

90. KCC's medium term planning needs to be seen in the context of Kent's housing growth and consequent wider infrastructure and investment needs. This is set out in "What Price Growth". The scale of development being sought by the Government will affect the whole of Kent and pose a huge financial challenge over the next 20 years. The Government has not yet fully recognised the scale of the investment in local services required by its plans for housing development in the South East.

91. KCC has been working with partners to assess the investment contribution that will be needed in the wider public sector to meet the scale of the growth in the county. We have developed models to assist in this assessment of our investment needs and the revenue impact of that investment. It is this context that we will continue to be urging the government that data on population numbers should be projected where possible for growth areas, and that any time lags should be avoided if at all possible.

92. The County Council will work together with the Government and across the public sector to maximise funding streams from other investment sources such as PFI and PPP where these offer value for money, as well as exploring Kent retaining a proportion of the additional business rates generated by new commercial development.

93. KCC's decisions on our Medium Term Capital Programme must be weighed against the scale of the Government's continuing support for borrowing and grant funding, the new prudential borrowing regimes, and the County Council's total borrowing and our ability to service this through revenue funding.

94. Some specific service issues affect authorities such as KCC. The shortage of land in the South East affects waste management costs, through higher capital costs of new facilities for recycling and incineration, as well as land fill.

95. The Government's "Building Schools for the Future" programme, which aims to transform the property estate of secondary schools, has seen initial work in Kent begin in 2007, KCC having been announced as part of tranche 3 of the programme. This has occurred because our educational performance (assessed by % of 5 A*-C at GCSE), is in the top quartile.

96. Over the past six years, in particular, the level of capital expenditure provided for by the government in public expenditure plans has increased significantly, particularly for building works at schools. At the same time, however, there has been a marked swing towards borrowing rather than capital grant, to pay for this welcome investment. In 1994-95 borrowing accounted for 59% of government capital approvals but by 2003-04, just prior to

the introduction of Prudential Borrowing, that had risen to 74% of approvals. The majority of capital expenditure based on government capital directions is therefore in the form of supported borrowing rather than government capital grant. This has obviously had a direct impact upon KCC's level of debt.

97. A further point to note on capital financing is that the revenue costs of the debt are picked up through the Capital Financing component of grant. However, on average only about 90% of the increase in borrowing is met through increased grant, leaving some 10% to fall on council tax. If, as anticipated, KCC receives only a floor level increase in grant next year, any increase in the cost of borrowing is all likely to fall on council tax.

Financial Planning Risks

98. All our resourcing and spending assumptions are based on the Government's expressed views about levels of council tax, increases in government grant and funding for Kent schools.

99. This year we face considerable uncertainty over funding both for next year and the following few years. We have the following to take into account:

- CSR07
- Uncertainty of whether a floor funded authority
- Uncertainty over formula grant changes
- Uncertainty over specific grant changes
- Size of the unfunded spending pressures growing each year (to £1,206m in 2017-18)
- On-going risk of not recovering costs of supporting Asylum Seekers.

100. There is uncertainty over the burdens that may be imposed upon local government by a number of new bills before parliament:

- Housing and Regeneration Bill
- Health and Social Care Bill
- Children in Care Bill
- Education and Skills Bill
- Planning Reform Bill
- Planning Gain Supplement Bill
- Climate Change Bill
- Local Transport Bill
- Criminal Justice Bill
- Coroner's Bill

101. There is a risk to the LABGI scheme. KCC has argued the current scheme is not operating as it should do. Other authorities, with specific issues, have gone further and sought judicial review of the government's operation of the scheme. On 31 July 2007, two councils won their judicial review that the government had not operated the scheme correctly. Government has undertaken to resolve the uncertainties that this now causes but we await further detail of how exactly this will be resolved.

102. Our key assumptions on the budget and medium term plan for the County Council are therefore:

- 0% grant increase for each of the next three years given the likely constraints imposed upon us by CSR 07 and the three year local government finance settlement
- 5% maximum increase in council tax per annum given the threat of capping

- Council Taxbase grows by 1% per annum
- 2% limit on pay having due regard to the Chancellor of the Exchequer's stipulation to all pay review bodes that public sector pay increases must be contained within that limit.
- That specific grant changes and risks do not adversely move against us, but if they do and funding is directly reduced, we will have no option but to reduce services
- That Dedicated Schools Grant is sufficient to meet all government promises on service extension and minimum funding guarantees
- That costs of asylum seekers are fully met and reimbursed by government
- That we have fully captured updated pressures on our services (pay, prices, demographics, legislation)
- That resources are aligned to policy priorities
- That we deliver significant efficiencies and savings in specific services and through a series of cross cutting reviews of services

103. Taking these assumptions we anticipate that the overall budget position will be as follows

	2008-09	**2009-10**	**2010-11**
	£'000	**£'000**	**£'000**
Base budget	744,266	771,189	803,988
Base adjustments	494	0	0
Pressures (see Appendix 2)	66,515	67,614	66,049
Savings and Income Generation	-40,086	-34,815	-31,221
Budget Requirement	**771,189**	**803,988**	**838,816**

104. Cash limits for individual portfolios will be set having due regard to our policy priorities. Our priorities will have due regard to spending pressures, demographic change, legislative imposition and local choice. The indicative pressures listed in appendix 2 will be scrutinised very closely as we go through the budget process. There will inevitably be changes to this as that process develops.

105. The overall scale of the gap between what we would wish to spend and what we are likely to be able to afford, and the consequential savings target, is likely to be consistent with the overall 3%, government imposed Gershon target over the medium term (estimated at around £104 million, in appendix 3).

Reserves

106. The Director of Finance is required to consider the adequacy of the authority's reserves as part of the budget process. Our existing strategy is to take a view about the balance of risk on our medium term financial plans in order that we maintain sufficient levels of reserves to meet such risks. It is our view that with £25.8m of general reserves (at 31 March 2007) this is achieved but will be reviewed, as normal, during the budget process.

Appendix 1 – Timetable

Key Milestone Dates

What	***Who***	***When***
Autumn Budget Statement	Cabinet	17 September
Opportunity for Cabinet Scrutiny to consider Autumn Budget Statement	Cabinet Scrutiny Committee	27 September
Public consultation on budget	Cabinet Member for finance, finance officers, MORI, district council representatives	22 & 29 September
Respond to formal consultation on formula grant changes	Budget IMG, Cabinet	10 October
Comprehensive Spending Review 2007 announced by government then analysis and interpretation for impact on KCC 2008-11	Cabinet	15 October (*timing not yet announced by government)*
Review of budget proposals and overall pressures, impacting upon the relevant directorates	Policy Overview Committees	7 – 20 November
Provisional Settlement – announcement by government and then analysis and interpretation for impact for KCC 2008-11	Financial Strategy Group – briefing for all members	Late November / early December (*timing not yet announced by government)*
Update on Provisional Settlement and review of corporate budget strategy (if announced - see above entry)	Cabinet	3 December
Chancellor of Exchequer Pre-Budget Report	Financial Strategy Group	December (*timing not yet announced by government)*
Budget proposals published and press conference	Cabinet	21 January
Review of budget proposals and overall pressures, impacting upon the relevant directorates	Policy Overview Committees	25 – 31 January
Final settlement for 2008-09	Cabinet	Late January/ early February (*timing not yet announced by government)*
Opportunity for Cabinet Scrutiny to consider proposed budget	Cabinet Scrutiny Committee	1 February
Cabinet recommends budget to Council	Cabinet	6 February
Council sets budget and precept	Council	19 February

Appendix 2 – Indicative Pressures

	2008-09	2009-10	2010-11
	£'000	£'000	£'000
Existing pressures			
Pay	8,869	7,673	0
Prices	15,626	17,390	0
Government/Legislative	8,181	5,771	0
Demand/Demographic	4,525	5,738	0
Towards 2010	5,165	3,350	0
Schools Budget	33,850	20,072	0
Dedicated Schools Grant Increase	-38,187	-26,449	0
Service Strategies and Improvements	13,104	15,167	0
Sub-total	**51,133**	**48,712**	**0**
Major new pressures			
Prices – Private and Voluntary sector purchasing Increased prices	534		
Prices – impact of freedom pass	300		
Government - Looked After Children pledge	1,401		
Government - Early years pressures	1,259		
Government - Care Matters	911		
Legislative - Landfill Tax escalator	950	950	950
Demand – residential care	1,000		
Demand - Other fostering pressures	537	233	
Demand - Increased demand for Adult Services	3,354	2,602	
Demand - for Coroners/YOS services	300		
Service Strategies and Improvements - Increased Highways spending	5,000		
Service strategies and Improvements – Corporate Communications	350		
Service strategies and Improvements - Financing capital programme		5,615	10,000
Pay new year provision			9,392
Prices new year provision			15,024
Legislative new year provision			7,351
Demand new year provision			7,924
Schools Block new year provision			28,036
DSG new year provision			-35,903
Expected pressures to emerge - not yet fully identified		10,000	23,400
Other changes – net impact including revisions to existing pressures	-514	-498	-125
Total pressures	**66,515**	**67,614**	**66,049**

Appendix 3 – Assumed savings requirement at 3% (Gershon) per annum

	2008-09 £'000	2009-10 £'000	2010-11 £'000
Operations, Resources and Skills (CFE)*	4,875	4,875	4,875
Children, Families and Educational Achievement*	3,989	3,989	3,989
Adult Services	12,822	12,822	12,822
Environment Highways and Waste	4,073	4,073	4,073
Regeneration and Supporting Independence	314	314	314
Communities	2,991	2,991	2,991
Public Health	0	0	0
Corporate Support	1,418	1,418	1,418
Policy and Performance	115	115	115
Finance	4,193	4,193	4,193
Indicative Gershon savings target	**34,790**	**34,790**	**34,790**

* These reflect new titles for CFE portfolios – likely to be further virements between the two portfolios as detailed budgets and responsibilities refined.

The savings requirements are calculated as 3% of gross 2007-08 budgets. Adjustment has been made to the education targets to **exclude** savings expected to be contained within Dedicated Schools Grant. These are estimates in advance of the publication of the government's updated Efficiency Technical Note which will set out detail on the overall target required.