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To: **Policy & Resources Cabinet Committee** – 2nd February 2018

Subject: Budget 2018-19 and Medium Term Financial Plan 2018-20

Classification: Unrestricted

Summary: County Council received a report on the Autumn Budget Statement on 19th October 2017. That report set out an update to the Medium Term Financial Plan (MTFP) for 2018-19 and 2019-20 including progress on proposals to resolve the unidentified gap in the original plan. The report marked the start of a communication and consultation campaign to support decisions on the final budget in February. It also granted authority to Corporate Directors to start to make the necessary arrangements to be able to deliver savings once the final budget has been approved and to develop further proposals to resolve the gap and deal with uncertainties.

The final draft budget proposals were published on 15th January 2018 to support the scrutiny and democratic process through Cabinet Committees, Cabinet and culminating in the annual County Council budget setting meeting on 20th February. This report provides Policy and Resources Cabinet Committee with an opportunity to comment on the draft budget proposals and make recommendations to Cabinet Members as part of this process

Members are asked to bring to this meeting the draft (black combed) 2018-19 Budget Information and 2018-20 Medium Term Financial Plan document published on 15th January 2018.

Recommendations:

Members of the Policy and Resources Committee are asked to:

- a) NOTE the draft budget and MTFP, including responses to consultation and government provisional settlement
- b) SUGGEST any changes which should be made before the draft is presented to Cabinet on 5th February and full County Council on 20th February

1. Introduction

- 1.1 The Local Government Finance Act 1992 requires the Council to consult on and ultimately set a legal budget and council tax precept for the forthcoming financial year, 2018-19. The accompanying draft Budget Information and MTFP document (hereafter referred to as the Budget Book) sets out the detailed draft proposals. This document is designed as a reference document and includes a number of sections/appendices. This report is produced as a guide to help navigate the document.
- 1.2 The democratic process through Cabinet Committees, Cabinet, and ultimately full Council is the culmination of the budget setting process which takes almost a year to evolve beginning almost immediately after the budget is approved in February. This starts with the forecasts for the forthcoming year(s) in the MTFP presented at the same time as the budget. These are based on estimates and subject to continual revision and refinement. The MTFP usually has an unidentified savings gap for the future years which needs to be resolved.
- 1.3 In the last two years we have reported an interim update of the MTFP to County Council through the Autumn Budget Report. This includes updates to the forecasts and progress on identifying solutions to the unresolved gap. This also marks the launch of formal consultation as required under the Council's constitution and necessary to set a legal budget and council tax. The draft budget published in January for the final democratic process reflects the response to this consultation, further updates to forecasts, and final proposed resolution of any outstanding gap. Even then, this final draft can be subject to further changes leading up to the full Council meeting in February (including any amendments agreed at the meeting).
- 1.4 The final approved budget and MTFP is published in March.

2. Fiscal Context

- 2.1 The national fiscal context is an important consideration for the Council in setting the budget. This context does not just determine the amount we receive through central government grants but also sets out how local government spending fits in within the totality of public spending. This latter aspect essentially sets the government's expectations of how much local authorities will raise through local taxation. This element of locally financed expenditure is part of the annually managed expenditure (AME) portion of public spending and the government grant funded expenditure is part of the departmental resource spending (RDEL).
- 2.2 The public spending plans are set out in the quarterly Economic and Fiscal outlook from the Office for Budget Responsibility (OBR). The OBR is an advisory body established in 2010 to provide independent analysis of the public finances as background to policy decisions taken through the annual UK Budget. Section 2 of the Budget Book provides a summary of

the key aspects of the November economic and fiscal outlook report from the OBR including relevant extracts and charts.

- 2.3 The November 2017 OBR economic and fiscal outlook included a section dedicated to forecast of local authority spending. This part of the OBR report has been reproduced in full under paragraph 2.28 in the Budget Book (pages 19 to 27). In summary the OBR concluded that in the years up to 2015-16 local authorities had been able to underspend and add to reserves (despite the austerity programme and real terms reductions in budgets), but since then and for the foreseeable future it expects that authorities would need to draw down from reserves in response to rising spending pressures and reductions in real terms spending power. The OBR also predicted that spending on social care will absorb an increasing portion of councils' budgets, and capital spending would need to be funded by additional prudential borrowing. These key trends predicted by the OBR closely match KCC's experience and future forecasts.
- 2.4 The timing of the UK annual budget has been switched from March to the autumn. This should help our budget planning and means UK government tax and spending plans will be set for the forthcoming year before councils set their budgets. The autumn 2017 Budget announcement on 22nd November included very little to affect local authority spending plans.
- 2.5 The provisional local government finance settlement was announced on 19th December. This announcement is one of the key elements of the budget process as it includes several significant grants and council tax referendum principles. KCC submitted its response to the provisional settlement on 15th January.
- 2.6 In previous years the settlement has included significant changes to the distribution of government grants. The 2018/19 settlement had only minor changes to the indicative allocations in the 2017/18 settlement. This included further substantial reductions to the Revenue Support Grant (reduced from £66.5m to £37.6m), the removal of £15.2m worth of transitional grants, and the second year of reform of New Homes Bonus grant (with loss of £2m for KCC). This £46.2m loss of government grants in the settlement is part of the £113m budget gap.
- 2.7 There are also some grant increases in the settlement including; planned increases in the Improved Better Care Fund (iBCF), indexation of the 50% business rate retention, and additional compensation for the changes to Business Rates announced in the autumn 2017 Budget. The 2018/19 settlement also included the announcement of 10 new area areas to pilot 100% business rate retention (including Kent and Medway), and increases in the amount of council tax than can be raised without a referendum (from 2% to 3% for all local authorities and up to £12 for Police & Crime Commissioners).
- 2.8 The local government finance settlement shows a presentation of a core spending power for all authorities. This sets out the main sources of funding for all local authorities (council tax, retained business rates and government grants) each year between 2015/16 and 2019/20 i.e. the

current Spending Review and four-year settlement for those authorities taking up the offer. The 2018/19 core spending power does not include the additional business rates retention for pilot authorities.

- 2.9 The core spending power does not quite cover all the funding which makes up KCC's net budget requirement but does include the principal sources, however, it is useful for inter authority comparisons on a consistent like for like basis. The core spending power for all authorities can be found under paragraph 2.29 of the Budget Book (page 28), and KCC's individual calculation is shown in paragraph 3.10 (pages 51 and 52)

3. Revenue Budget and Medium Term Financial Plan Proposals

- 3.1 In order to meet the legal requirement to set a balanced budget the Corporate Director of Finance must be satisfied that it is based on robust estimates and includes adequate provision for reserves to cover risks and uncertainties. The 2018/19 draft budget includes £55.5m of additional spending demands (realignment of existing budgets plus forecasts for future demand and cost increases) and £11.4m to replace the use of one-offs on the 2017/18 base budget. This £66.9m of spending demands together with the £46.2m of government grant reductions (referred to in paragraph 2.6) make up the total £113.1m budget gap for 2018/19.
- 3.2 These spending demands have increased from the £58.8m forecast in the Autumn Budget report to County Council on 20th October. This increase is largely due to the need to include a higher provision for realignment of 2017/18 budget based on the most up to date forecasts. This includes a substantial provision of £12m held unallocated for a range of emerging issues where the full impact is still subject to further evaluation and/or it is still uncertain whether all the issues will need to be reflected in 2018/19 budgets. This provision covers issues such as further potential demand for social care placements, energy price volatility, impact of recent judgements on sleep-in payments, etc. In total we estimate these could amount to between £6m to £18m and thus £12m represents mid cost.
- 3.3 The spending changes also include minor changes to price increases and demographic demand based on updated forecasts, and more significantly a revision to the amount set aside a minimum revenue provision (MRP) to cover the capital finance requirements over the lifetime of capital assets. This MRP does not represent a change to the Council's policy (see appendix C of the Budget Book) but merely a recalculation of the amount needed for current and future years based on asset values/lifetime and the draft capital programme.
- 3.4 The 2018/19 draft budget includes savings and income proposals of £53.3m. This is slightly less than the £54.5m identified in the Autumn Budget Report to County Council and means the unidentified gap of £8m in that report is now no longer an issue. The reduced savings are possible following the additional flexibility in the provisional settlement (100% business rate pilot and higher council tax referendum threshold) combined with a higher than forecast council tax base and in year collection fund

balance, and compensation grant for the CPI indexation of retained business rates in 2018/19.

- 3.5 The main savings plans which have been revised downwards are from transformation programmes and policy savings. Efficiency savings, income generation and financing items have all increased a little. The increase in financing savings comes from the recalculation of MRP described in paragraph 3.3. The financing savings include £5.1m drawdown from the Council's central reserves and £6.3m from directorate reserves. As in previous plans, draw down from reserves creates an additional pressure in future years as this is only a one-off solution.
- 3.6 As identified in paragraph 2.7, the funding includes some grant increases (amounting to £15.2m). This leaves a total of £44.6m extra which needs to be raised through council tax and the locally retained share of business rates to balance the net budget requirement. The draft budget proposed this is raised as follows:
- £13.4m increase in the council tax base due to increase in the estimated number of households liable to pay council tax and reducing application of council tax districts as notified by district councils
 - £19m from the proposed increase in council tax up to but not exceeding the new 3% referendum threshold
 - £12.7m for the proposed additional 2% social care levy (the draft budget does not include the additional flexibility to raise up to 3% in any one year but no more than 6% over 3 years – this flexibility is assumed in the core spending power calculations for 2018/19 and 2019/20)
 - £6.5m reduction in the estimated collection fund balances – this is a KCC estimate pending notification of the estimated balances from all district councils
 - £6m increase in the locally retained share of business rates including the 3% CPI indexation and KCC's estimated share of the 100% retention pilot – this estimate will need to be revised when we have received the business rate tax base notifications from district councils
- 3.7 For multi-year consistency we have presented KCC's RSG and business rate top-up in 2018/19 as if the 100% pilot did not exist. As described in paragraph 3.6 we have shown the estimated additional proceeds for KCC from the pilot in the retained local share of business rates. This is consistent with the presentation in the core spending power and the presumption in the Kent and Medway pilot bid that all authorities will receive the same as they would have received under the 50% arrangement and current pool, with any remaining additional proceeds distributed according to the K&M agreement.
- 3.8 The 2018/19 settlement shows a notional distribution of all of the additional business rate retention to the upper tier authorities (KCC and Medway). This switches these authorities from receiving top-up to their business rate share to paying a tariff back to central government from the additional retention. The published settlement also includes RSG to be funded from the additional locally retained business rates for all pilot

authorities (revising their tariff/top-up equation) and Rural Services Delivery Grant for one Kent authority. This complexity is not reflected in the draft budget as it has no overall effect on the net budget requirement and makes multi-year comparisons difficult.

- 3.9 The draft budget proposals are summarised paragraphs 1.8 to 1.12 in section 1 (Executive Summary) of the Budget Book (pages 4 to 6). The council tax proposals are summarised in paragraphs 1.16 and 1.17 (page 7) and section 8 (pages 103 to 105). Fuller detail is included in section 3 (Revenue Strategy). All the calculations set out in sections 10 and 11 (pages 129 to 144) and appendix A.
- 3.10 The provisional 2019/20 plan is presented at a high level for the whole council in appendix A(i). As identified in paragraph 3.5 this includes £15m additional pressure to replace one-offs in the 2018/19 draft budget, including the drawdown from central and directorate reserves and the flexibility to use capital receipts to fund revenue costs of service transformation. The 2019/20 plan includes forecasts for further spending demands and the full year effect of existing savings plans.
- 3.11 The 2019/20 funding is based on the indicative 2019/20 figures in the 2018/19 provisional settlement. It assumes the 100% business rate pilot is a one-off in 2018/19, and assumes 1% forecast growth in the tax base and provisional 2% increase in council tax plus the final 2% social care levy. This leaves some headroom within the referendum levels.
- 3.12 The 2019/20 plan has a total of £10.2m of unidentified savings, this is not uncommon and represents a lower target than we have had unidentified in the recent past.

4. Budget Consultation

- 4.1 As described in paragraph 1.3 consultation on the Council's revenue budget and council tax proposals was launched on 12th October to coincide with the publication of the Autumn Budget Report to County Council. This consultation sought views on council tax and KCC's budget strategy. The consultation was web based supported by a social media campaign. This represented an innovation on previous years aimed at increasing engagement at lower cost. This was achieved with a much higher volume of web page views (particularly from external users) and increased number of responses.
- 4.2 A summary of budget consultation is included in paragraphs 3.31 to 3.35 of the Budget Book (pages 56 to 57) and comprehensive report on consultation activity and responses is published on the Council's website (see link in background documents).

5. Capital Budget

- 5.1 The Budget Book also includes the Council's proposed capital investment programme for 2018/21. The programme is derived from the Council's capital strategy set out in section 4 of the Budget Book. This strategy seeks to balance the need to invest in improving assets with affordability, with particular regard to the long-term impact on the revenue budget from taking up additional prudential borrowing to fund projects. Each £10m of borrowing costs around £0.8m per annum in debt servicing costs for the next 25 years.
- 5.2 The planned capital spending over the next 3 years (2018-21) is £794.7bn. This includes the following major areas of investments:
- School maintenance, improvements and expansions £341.7m
 - Roads and infrastructure £261m
 - Grants and advances £44.2m
 - IT systems £14.4m
 - Equipment and vehicles £0.1m
 - Land and buildings £130.8m
 - Capital investment in transformation costs £2.5m
- 5.3 For the forthcoming programme we set an overall limit that additional borrowing should not be more than £100m over the next 3 years. This was based on assessment of overall affordability against forecast capital demands. This has enabled a number of new projects to be included in the programme including providing additional school places to supplement central government basic need funding, essential investment in the Council's buildings and road infrastructure to ensure these continue to be safe to use, investment in additional extra care capacity for social care clients, and forward funding a number of projects to promote economic development.
- 5.4 The capital programme is funded from a number of sources in addition to prudential borrowing. This includes central government grants for schools, roads and economic development, developer contributions, and receipts from the sale of surplus assets. The provision of school places remains the biggest risk to the capital programme assumes we will be able to agree additional central government grant to support the establishment of new schools and expansion of existing schools.

6. Finalising the Budget

- 6.1 It is almost inevitable that there will be some further changes before the budget and council tax is presented to County Council for approval on 20th February. At the very minimum this draft is based on provisional council tax base estimates from districts, and KCC's estimate for the local share of business rates and collection fund balances. It is almost certain that these estimates will change for the final approval. We also need to leave scope to deal with any late issues which may arise, including recommendations from Cabinet Committees.

- 6.2 At this stage we plan to deal with any changes to the published draft through the report to County Council rather than re-issuing the draft budget. However, depending on the number and complexity of the late changes this may be reviewed.

7. Recommendations

Recommendations:

Members of the Policy and Resources Committee are asked to:

- a) NOTE the draft budget and MTFP, including responses to consultation and government provisional settlement
- b) SUGGEST any changes which should be made before the draft is presented to Cabinet on 5th February and full County Council on 20th February

8. Background Documents

- 8.1 KCC's Budget webpage
<http://www.kent.gov.uk/about-the-council/finance-and-budget/our-budget>
- 8.2 KCC's approved 2017-18 Budget and 2017-20 Medium Term Financial Plan
http://www.kent.gov.uk/_data/assets/pdf_file/0006/66534/budget-book-2017-18.pdf
<http://www.kent.gov.uk/about-the-council/strategies-and-policies/corporate-policies/medium-term-financial-plan>
- 8.3 Autumn Budget Report to County Council 19th October 2017
<https://democracy.kent.gov.uk/documents/s79227/Item%20%20-%20Autumn%20Budget%20Statement.pdf>
- 8.4 KCC Budget Consultation launched 12th October 2017
<https://consultations.kent.gov.uk/consult.ti/BudgetConsultation2018/consultationHome>
- 8.5 Chancellor's Autumn Budget 2017 22nd November 2017
<https://www.gov.uk/government/topical-events/autumn-budget-2017>
- 8.6 Office for Budget Responsibility fiscal and economic outlook 22nd November 2017
<http://obr.uk/efo/economic-fiscal-outlook-november-2017/>
- 8.7 Provisional Local Government Finance Settlement 19th December 2017
<https://www.gov.uk/government/collections/provisional-local-government-finance-settlement-england-2018-to-2019>
- 8.8 KCC Draft Budget Book 15th January 2018

http://www.kent.gov.uk/_data/assets/pdf_file/0005/78170/Draft-BB-and-MTFP-Black-Combed-Version-10012018-FINAL.pdf

http://www.kent.gov.uk/_data/assets/pdf_file/0006/78171/Budget-Exec-Summary.pdf

9. Contact details

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