

CABINET

18 OCTOBER 2022

FINANCIAL OUTLOOK 2023/24

Portfolio Holder: Councillor Alan Jarrett, Leader of the Council

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Summary

This report sets out our projections of the Council's income streams alongside the initial assumptions around pressures on the cost of services insofar as they impact the 2023/24 budget.

1. Budget and policy framework

- 1.1. It is the responsibility of Cabinet, supported by the management team, to develop a draft revenue budget. This report identifies the key issues that need to be addressed as part of that budget preparation.

2. Background

- 2.1. The Financial Outlook 2022/23 was considered by the Cabinet in September 2021 and projected a potential budget gap for the Council of £33.010million. During the following months the projections were refined based on the latest activity data, challenging costs and reassessing the trends projected. That work had reduced the potential gap to £18.176million by the time the Draft Budget was presented to the Cabinet in November 2021. The provisional Local Government Finance Settlement resulted in £2.455million additional resources compared to the Draft Budget projections, and Officers and Portfolio Holders worked to develop a package of solutions to mitigate the remaining pressures. The proposed budget presented to Full Council in February still exceeded the available resources by £3.896million, with the final budget agreed requiring the contribution from general reserves of £4.853million.

3. Income projections

3.1. Government grant

3.2. While the Spending Review 2021 set out in October 2021 set government departmental budgets for the three years up to 2024/25, in order to “prioritise certainty for 2022/23” instead local government received a one-year finance settlement. Speaking at the Local Government Association Conference in late June 2022, the then Chancellor Michael Gove said that a two-year settlement would be introduced ‘next year’ (covering 2023/24 and 2024/25) and that a consultation would be launched ‘shortly’ likely before parliament recess.

3.3. The Conservative leadership contest concluded with Liz Truss becoming the Prime Minister, and on 23 September the new Chancellor of the Exchequer, Kwasi Kwarteng, unveiled his Growth Plan in a fiscal event widely reported as a ‘mini budget’. The key impacts for local authorities were as follows:

- The reversal from November 2022 of the 1.25% increase in National Insurance contributions for both employees and employers that was implemented on 1 April 2022 as the Health & Social Care Levy. While this represents a reduction in required expenditure, local authorities were funded for the cost of employers contributions through the local government settlement for 2022/23, therefore it is anticipated that government grant will reduce by a commensurate amount from 2023/24.
- The announcement of the Energy Bill Relief Scheme, which is open to all non-domestic contracts for energy supply including public sector organisations, and will deliver a discount based on the difference between the estimated wholesale portion of the unit price and a baseline ‘government supported price’. No further details have been published at this stage.
- In a move that could in future impact the Council’s trading companies Kyndi and Medway Development Company, the planned increase in corporation tax in corporation tax has been cancelled.

3.4. A series of announcements have also been made outside the fiscal event on 23 September:

- On 22 September the Secretary of State for Health and Social Care Therese Coffey published a policy paper; ‘Our Plan for Patients’ and announced a new £500million Adult Social Care Discharge Fund as a “first step [to] inform our further action from next year to rebalance funding across health and care”. This grant is estimated to represent an additional c£2million for Medway for the current financial year, and while the tone of the announcement suggests this will be followed with further funding in future years this has not been confirmed.
- On 3 October the Chancellor confirmed that a new fiscal statement would be brought forward from the 23 November to a date in October.
- On 4 October the Chancellor confirmed that there will not be a Spending Review this year due to a lack of time; this means Departmental budgets for 2023/24 will not be increased to reflect

inflation, and as such the local government finance settlement will effectively deliver a real-terms cut.

3.5. At the time of writing no further announcements on the public finances have been made. It is therefore considered likely that the long-awaited major reforms to local government funding, including changes to the mechanism through which national allocations are distributed to local authorities based on relative needs and resources and the reflection of the 2021 Census data, will be delayed to 2025/26 or replaced altogether.

3.6. Our projection therefore is a roll-over settlement with the same national grant allocations, distributed via the same methodologies as the 2022/23 settlement adding no additional resources to the council's budget.

3.7. **Social Care Reforms funding**

3.8. Alongside the Spending Review 2021 the government launched its reforms for health and social care and the local government allocations for the first three years of the Department for Health and Social Care's Market Sustainability and Fair Cost of Care Fund. In 2022/23 Medway received £674,000 from a national allocation of £162million, and therefore based on the national allocations for 2023/24 (£1.4billion) and 2024/25 (£2billion) we expect to receive in the region of £5.8million and £8.2million respectively. While the new government have not made any official statements as to the continuation of the Adult Social Care Reforms, work progresses at a Departmental level. It is understood that the changes will go forward, but be funded from general taxation/borrowing now the Health & Social Care Levy on National Insurance has been reversed. On the assumption that these reforms go ahead in the current form under the new Prime Minister, once confirmed, these sums will be added to the budget for Adult Social Care however it is assumed this funding will only cover the new burdens arising from the reforms and will not help to close the Council's budget gap.

3.9. **Income from Local Taxation – the Collection Fund**

3.10. Income from Council Tax and Business Rates is held in a ringfenced collection fund account, from which authorities draw the budgeted level of income in each year irrespective of actual income collected. Any shortfall on income collected compared to that budgeted level results in a collection fund deficit which is recovered by reducing the amount of income the Council can budget for in the following year.

3.11. Given the scale of deficits expected owing to the pandemic, in 2020 the then Chancellor announced that repayments to meet collection fund deficits accrued in 2020-21 in respect of Council Tax could instead be phased over a three-year period from 2021/22 to ease immediate pressures on budgets. Therefore 2023/24 is the final year impacted by this deficit spreading, which reduces the amount of income available to the Council from the collection fund in 2023/24 by £2.053million. There has been no indication from the government that any other support for collection fund losses will be provided

for 2023/24 and therefore no additional support is included in our current projections.

3.12. **Council Tax**

- 3.13. The Council Taxbase refers to the number of Band D equivalent dwellings in a local authority area and is used to determine the level of council tax an authority charges each dwelling. To calculate the tax base for an area, the number of dwellings in each council tax band is adjusted to take account of any discounts, premiums or exemptions. The resulting figure for each band is then multiplied by its proportion relative to Band D (from 6/9 for Band A to 18/9 for Band H) and the total across all eight bands is calculated. Despite the continued regeneration of Medway, the impact of the Covid-19 pandemic had reduced the Council's Taxbase for 2022/23, after many years of successive growth. Increases in the number of claims for Local Support for Council Tax and higher than anticipated levels of Single Person Discount were the primary drivers of this reduction at Medway.
- 3.14. The Council's financial planning advisors are projecting that our taxbase will grow for 2023/24 to 89,441.36 band D equivalents, an increase of 1.59% broadly in line with pre-pandemic historical growth which averaged around 1.4%.
- 3.15. The government have to date made no announcements about the ability of local authorities to increase the Council Tax and as such, it is assumed that the 2023/24 settlement will allow the Council to increase this within the historic referendum limit of 2%.
- 3.16. At the end of the 2020/21 financial year, there was a deficit of £5.774million on the Collection Fund in relation to Council Tax. Of this figure the Council is required to repay the final £2.053million through the 2023/24 budget.
- 3.17. Therefore at the projected taxbase of 89,441.36 with 2% increase and after repayment of the deficit, the Council's projected income would be £143.153million representing £5.067million additional resources.

3.18. **Business Rates**

- 3.19. The business rates retention system introduced in 2013 was designed to transfer a level of risk and reward to local authorities, as it means growth or decline in the local economy impacts the council's income. Under the current system most local authorities retain 50% of rates collected (at Medway Council this is 49% with 1% paid to Kent Fire Authority) with the balance paid to the Government. The government has set a baseline funding level for each authority and for each year calculates a business rates baseline. Where an authority's business rates baseline exceeds its funding baseline, they pay the difference to central government as a tariff, which is used to pay for a top-up for authorities whose funding baseline is less than its business rates baseline. These tariffs and top-ups are updated each year by the business rates multiplier, now CPI.

- 3.20. The amount of income the Council can expect to receive in respect of the coming financial year is calculated at the end of January through a statutory return to the government called the NNDR1. This calculation reflects any deficit or surplus in actual income received to the fund compared to the previous year's budget, the total income expected through Section 31 grants compensating for rate reliefs awarded by the government, the top-up grant to ensure authorities reach the baseline funding level set by the government, and the total Rateable Value (RV, as set for each non-domestic property by the Valuation Office Agency) of the area.
- 3.21. The change in the total RV in Medway between the end of January and the end of the following financial year (a period of 14 months) between since January 2018 is shown in the table below.

	January estimated RV in advance of financial year	Actual RV as at end of financial year (*2022-23 as at June 2022)	RV change
2018-2019	226,801,200	231,816,956	+2.21%
2019-2020	229,022,911	230,379,494	+0.59%
2020-2021	229,803,547	229,567,388	-0.10%
2021-2022	228,917,468	227,238,654	-0.73%
2022-2023	226,974,397	228,264,330*	+0.57%

- 3.22. While previously the business rates base in Medway had grown year on year, despite the government meeting a significant proportion of liabilities through rates relief and grants throughout the pandemic, adverse impact on the total RV is clear in 2020/21 and 2021/22. One significant new non-domestic property has been added to the RV since January 2022 accounting almost entirely for the RV change between January and June 2022 and we are not anticipating any further significant growth during the remainder of the year.
- 3.23. Collectively our advisors are projecting that the total income to Medway Council through retained business rates, Section 31 Grant and top up grant in 2023/24 will be 8.78% higher than in 2023/24, representing an increase of £5.134million.

4. Expenditure projections

4.1. Funding the inherent gap

- 4.2. The 2022/23 budget was balanced with the use of £4.853million of general reserves, which will need to be addressed in a sustainable way through the 2023/24 budget build and this (less the removal of one-off elements of the current year budget) is therefore the first call on the additional resources projected in section 3 of this report.

4.3. **Staff pay**

4.4. In previous years, Medway Council staff have received pay awards broadly in line with inflation; 1% in 2017/18, 1.5% in 2018/19 and 2% since 2019/20 though the initial planning assumption has been 1% for some years. Many lower paid staff have however received increases in excess of this resulting from increases in the National Living Wage rates and the increase of all Council staff to £10 per hour minimum from April 2022.

4.5. Government advisors the Low Pay Commission consulting on whether the national living wage should rise:

- to £10.32 (within a £10.14-£10.50 range) in April 2023 – an increase of between 6.7% and 10.5%.
- It may then go up to £11.33 for 2024, a rise of almost 20% in two years. Meanwhile, the age threshold for the national living wage is set to come down from 23 to 21 by 2024 at the latest.

If agreed, it is estimated that these increases would cost the Council £235,004 in 2023/24 and £849,994 in 2024/25.

4.6. On 20 July the government announced the pay deals covering public sector workers, including teachers, nurses, doctors, police officers, and members of the armed forces. Increases agreed range from 3.5% for senior military staff, with 5% the average increase, up to 9.3% for the lowest earners in the NHS.

4.7. The review of the MedPay structure is underway and it is anticipated that 10% of the Council's posts will be reviewed during 2022/23. While this is likely to bring additional costs as pay is uplifted in some areas, it is anticipated that overall the process will be cost-neutral as budgets for agency staff can be reduced as recruitment and retention of permanent staff improves.

4.8. The Council's annual staffing budget is £96.6million and as such every 1% increase in the permanent salary base would add £966,000 to the budget requirement and an increase of 5% for all staff would require the addition of £4.830million.

4.9. **Interest rates & minimum revenue provision**

4.10. The Council's ambitious and expansive capital programme currently stands at more than £472million of which almost £256million is funded from borrowing. The Council's Interest & Financing Budget funds the cost of interest payments to service this borrowing, with the current budget set at £10.445million.

4.11. In August 2022 the Council's Treasury advisors projected that Bank Rate will continue to rise to peak at 2.75% in March 2023, however other bodies including Capital Economics were projecting that peak would be 3%. Since August, there has been increasing volatility and the Bank of England's Monetary Policy Committee has increased Bank Rate from 1.75% to 2.25%. Our advisors now project that rates will continue to rise to peak at 5% in March 2023, will not begin to reduce until December 2023 and will not return to 2.75% until March 2025. On 30 September 2022 the ratings agency S&P

Global downgraded its outlook on the UK from Stable to Negative, with Fitch Ratings agency doing the same on 6 October. This indicates that the UK's credit rating could be downgraded, which would increase borrowing costs for the government. Since the majority of our borrowing is from the government via the Public Works Loan Board, this would further increase the cost of financing the Council's capital programme.

- 4.12. Where authorities borrow to finance capital spend, we are required under regulations to set aside money each year from the revenue account to make sure we can afford to repay the principal of the debt, known as the Minimum Revenue Provision (MRP). The Council's Interest & Financing budget also funds the cost of contributions to this provision.
- 4.13. The extent to which projected rate rises will impact the Council's borrowing is dependent on progress with the agreed capital programme. Based on the first round of budget monitoring, the projected cost of financing the programme as planned to the end of 2023/24 could exceed the 2022/23 budget by between £5million and £14.930million.
- 4.14. **Children's Social Care and Education**
- 4.15. The 2022/23 budget assumed 947 placements and reflected a 2% increase in weekly rates across all placement types. The Round 1 budget monitoring indicates that while internal fostering and supported accommodation placements are in line with the budgeted increase, rates for residential and independent fostering agency placements are costing between 5-15% more than budgeted. Funding this cost of current service in 2023/24 is projected to add £5.874million to the budget requirement.
- 4.16. Current projections of demographic growth increasing the number of placements would add a further £4.464million.
- 4.17. Every 1% additional price increase awarded to providers would add £336,000 therefore a 5% increase would add £1.680million while a 9.9% increase would add £3.327million.
- 4.18. The Council meets the cost of transporting pupils with Special Educational Needs and Disabilities (SEND) to school, however as reported in the first round of budget monitoring for 2022/23, the increase in pupil numbers seen in Medway and rising fuel costs have resulted in a forecast pressure of £2million in the current year. Our initial projections for further demographic growth and inflationary pressures on this service could see this pressure rise to £3.285million in 2023/24.
- 4.19. A programme of work is underway to resolve the deficit position on the Council's Dedicated Schools Grant reserve, including a review of expenditure charged to the Dedicated Schools Grant. This work has identified a range of services that must now be charged to the General fund and represent a pressure of £2.900million for 2023/24.

- 4.20. Therefore the Children's Social Care and Education budget pressure projected for 2023/24 is between £17.184million and £21.124million.
- 4.21. **Adult Social Care**
- 4.22. The 2022/23 budget assumed 3,027 placements and reflected a 3.8% increase in weekly rates for residential/nursing and supported living placements. The Round 1 budget monitoring indicates that rates being charged are between 5-6% higher than budgeted, an additional 1-2% cost. Funding this cost of current service in 2023/24 is projected to add £2.466million to the budget requirement.
- 4.23. Current projections of demographic growth increasing the number of placements would add a further £1.2million.
- 4.24. Every 1% additional price increase awarded to providers would add £854,000 therefore a 5% increase would add £4.268million while 9.9% would add £8.454million.
- 4.25. As set out in paragraph 3.8 of this report, we expect to receive in the region of £5.8million in 2023/24 through the Department for Health and Social Care's Market Sustainability and Fair Cost of Care Fund to meet the costs of the Adult Social Care reforms. Once confirmed, this sum will be added to the budget for Adult Social Care however it is assumed this funding will only cover the new burdens arising from the reforms and will not help to close the Council's budget gap.
- 4.26. Excluding the social care reforms funding/pressures, the Adult Social Care budget pressure projected for 2023/24 is between £5.846million and £12.593million.
- 4.27. **Inflation on contractual expenditure**
- 4.28. As at August 2022 the UK CPI rate was 9.9%. Inflationary uplifts are built into many of the Council's service delivery contracts and within the Regeneration, Culture & Environment Directorate there is a budget of £44.371million for services delivered through external contracts:
- Waste: £25.866million,
 - Transport: £5.805million,
 - Greenspaces/parks/cemeteries: £4.266million,
 - Highways: £2.208million,
 - Regulatory services: £0.532million,
 - CCTV: £0.688million,
 - Facilities Management: £5.005million.
- 4.29. A 1% uplift across these contracts would add a pressure of £443,710, therefore inflation at 9.9% this would represent the addition of £4.393million to the Council's budget requirement. The extent to which these are contractual will determine the opportunity with suppliers to reduce the impact of this on our budget.

4.30. Utilities

- 4.31. A combination of geopolitical, regulatory and supply factors have caused wholesale energy prices to increase rapidly from the second half of 2021 onwards, with the resultant energy price crunch projected to drive further significant increases in the cost of gas and electricity in the coming months. The Council's energy is purchased in advance through a consortium of local authorities whose bulk purchasing power has meant the Council's own energy costs have been somewhat insulated from these rises, in much the same way as households who had secured fixed deals with their providers have been. The first round of the Council's 2022/23 budget monitoring (reported to the Cabinet in August 2022) however projects utilities costs at c30% above budget and based on projections from the Council's utilities provider, the cost of our anticipated usage in 2023/24 could be double the current budget.
- 4.32. As set out at paragraph 3.3 of this report, the Chancellor announced the Energy Bill Relief Scheme that will provide support to public sector organisations, however no details have been published at this stage. Therefore our current estimate of the pressure that could arise from increasing utilities costs in 2023/24 is between £1-4million.

5. Conclusions

- 5.1. Our initial projections for income for 2023/24 amount to an increase in resources available of £16.001million. Our initial projections for the cost of services add a pressure of between £48.361 – £72.244million, therefore represent a potential budget gap for the Council of £32.626 – £56.243million.

Additional resources:	£million
Government grant	0.000
Social Care Reforms Funding	(5.800)
Council Tax	(5.067)
Business Rates	(5.134)
Total	(16.001)
Increased budget requirement:	
Funding the inherent gap	4.574
Staff Pay	4.830
Interest rates and Minimum Revenue Provision	5.000 – 14.930
Children's Social Care and Education	17.184 – 21.124
Adult Social Care reforms	5.800
Adult social Care	5.846 – 12.593
Inflation on contractual expenditure	4.393
Utilities	1.000 – 4.000
Total	48.361 – 72.244
Potential budget gap	32.626 – 56.243

- 5.2. We await the new Chancellor's announcements later in October for any further funding for local authorities. In the meantime, Portfolio Holders and

senior officers are working to identify a range of measures to balance the budget. Progress will be reflected in the Draft Budget 2023/24 which will be presented to the Cabinet in November.

6. Risk management

Risk	Description	Action to avoid or mitigate risk	Risk rating
Demographic Growth	Further demographic pressures may surface across social care above those assumed in our projections.	Close monitoring of demand for service to identify pressures early, robust budget monitoring.	C2 (Significant likelihood, major impact)
Social Care Reforms	The impact of the government's social care reforms may result in higher costs to the authority beyond that received through new burdens funding.	Officers continue to work to determine the impact of the reforms and lobby government for adequate financial support for the sector.	C1 (Significant likelihood, critical impact)
Special Educational Needs and Disabilities	Further increases in the number of children requiring support, and in the complexity of needs may surface above those assumed in our projections.	Close monitoring of demand for service to identify pressures early, robust budget monitoring.	C2 (Significant likelihood, major impact)
Inadequate funding	If the local government settlement does not provide sufficient funding, there is a risk to the future sustainability of the local authority sector.	Officers and Members continue to work closely to identify savings.	C1 (Significant likelihood, critical impact)

7. Consultation

7.1. Members are consulted on the development of the final budget as follows:

Initial budget proposals to Cabinet	15 November 2022
Reports to Overview and Scrutiny	December 2022 / January 2023
Budget proposals to Cabinet	7 February 2023
Budget proposals to Council	23 February 2023

8. Financial implications

8.1. The financial implications are set out in the body of the report.

9. Legal implications

9.1. The Council has a statutory duty to set a balanced budget no later than 11 March in the financial year preceding the one in respect of which the budget is set. When developing the budget, the Council needs to be cognisant that is required in law to provide some services, mandatory services, and others where it is a matter of local choice, discretionary services. It is a matter for the Council to determine what its local priorities are and those which are not. This can assist in determining resource allocation.

9.2. Paragraph 5.1 above refers to the potential budget gap for the next financial year. When determining its budget, the Council must have regard to the advice provided by the Chief Operating Officer (its statutory S151 finance officer). The S151 officer is required to report on the robustness of the estimates made for the purposes of the calculations, and the adequacy of the proposed financial reserves.

10. Recommendations

10.1. Cabinet is asked to note the initial forecast level of budget pressures and funding for 2023/24 and the projected budget deficit identified and to instruct the Corporate Management Team to bring forward proposals to address the projected budget deficit.

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Appendices

None

Background papers

None