

<b>Item No.</b> 23.	<b>Classification:</b> Open	<b>Date:</b> 14 July 2020	<b>Meeting Name:</b> Cabinet
<b>Report title:</b>		Policy and Resources Strategy: Financial Remit 2021-22 and Scene Setting	
<b>Ward(s) or groups affected:</b>		All	
<b>Cabinet Member:</b>		Councillor Victoria Mills, Finance, Performance and Brexit	

## **FOREWORD - COUNCILLOR VICTORIA MILLS, CABINET MEMBER FOR FINANCE, PERFORMANCE AND BREXIT**

This report begins the council's 2021-2022 budget planning process. It is dominated by huge financial uncertainties. Some of these existed prior to March 2020 - the challenges of ten years of austerity, the impact of welfare reform and the prospect of Brexit. However, since March, the impact of COVID-19 on our communities, services and finances has been acute and the route and length of recovery remains difficult for us to plot.

The budget process will culminate in setting the budget and council tax in February 2021. The budget and financial strategy also need to ensure resources align with the priorities emerging from refreshed Council Plan. The council has a statutory duty to set a balanced budget each year. Additionally, in order to ensure the council's finances are sustainable for the medium term, the report sets out the financial outlook and planning considerations for developing the council's medium term financial forecast for the following two years.

The report assesses the financial impact of Covid-19 and reviews other key financial assumptions and issues that the council needs to consider in making its plans for the period. The impact of Covid-19 on our communities and finances cannot be underestimated and the ongoing lack of clear and visible support from central government at the level required is increasingly concerning.

We have been through 10 years of financial austerity and now look set to face further significant turbulence as a result of the expected world-wide recession, continuing uncertainty over Brexit and over future funding of local government beyond 2021-22. Over the last decade we have focused on the delivery of our Council Plan and fairer future promises and we have developed fairer future budget principles to support the annual budget setting process. We have consistently promised value for money and committed to spending money as if it were from our own pocket. It is vital that we continue to maintain strong financial management at this time in order that we can do the best for our residents, communities and businesses.

The report sets out an approach for the budget process for 2021-22 to 2023-24 that takes account of the above and the requirement to identify savings options that fit within the overall policy and financial framework, aligning resources to the council's key priorities and approach to recovery and renewal.

At this stage there are a great many assumptions and uncertainties, and the financial and economic conditions are continually changing, along with the government response. In addition to an early estimate of £12.5m in respect of inflationary and pay pressures, including the revenue consequences of the council's ambitious capital investment programme, we continue to face demands and pressures on our services, particularly the High Needs Block of the DSG, where the deficit at 31 March 2020 was £18.5m, adult's and children's social care, homelessness, welfare support and other emerging pressures, for example lost contractual income.

This financial remit report is therefore being compiled in a period of unprecedented financial uncertainty. The report considers the most likely financial position to be faced by the council over the next three years. The forecast however includes a range of assumptions which may prove to be incorrect; sensitivity testing around these assumptions indicates a significant range of outcomes. The 'most-likely' projected funding gap for planning purposes is £26.2m in 2021-22, but this is in a range of £12.8m best case to £46.8m in the worst case.

Along with London Councils, we will continue to make the strongest case to the Government that they must meet their commitment to fully fund the council's costs in response to the pandemic and to use the next Spending Review to increase the overall level of funding for local government, to fully fund the cost implications of new burdens passed to councils over the last decade, to urgently address the pressures in social care, in children's services and across our schools and to address the unique pressures faced by London boroughs with regard to homelessness and No Recourse to Public Funds.

Despite the challenges, this administration remains determined to keep our promises, to protect and modernise our services and to maintain excellent financial planning that is more than fit for the future.

## **RECOMMENDATIONS**

That cabinet note:

1. The unprecedented financial uncertainties:
  - The impact of the Covid-19 pandemic on spending, income and savings plans and the pace of recovery;
  - The extent of government support to offset the financial cost to the council of the pandemic;
  - The expected world-wide recession as we emerge from lock-down and the end of the Brexit transition period;
  - The likely delay in the Spending Review intended to take place in 2020, with no indications of core funding and level of grants in 2021-22 and beyond;
  - The postponement of the planned reforms of local government finance (Fair Funding Review, Business Rate Retention arrangements) intended to be implemented from April 2021;
  - The likely deferment of Business Rates reset, planned for April 2021;
  - Governments proposals for sustainable long-term funding for Adult Social Care;
  - No confirmation of additional funding for new burdens and other demand pressures including social care, high needs costs, homelessness and impacts of welfare reform.
2. Economic and financial impacts to the council of Brexit remain unclear and that any local budget pressure may need to be contained within the limited budget and reserve created as part of the 2019-20 policy and resourcing strategy and budget for 2019-20;
3. That the accumulated deficit on the Dedicated Schools Grant was £18.5m at 31 March 2020 with the prospect of achieving any meaningful reduction without additional funding from the Department for Education being remote;
4. That financial planning is extremely challenging, with a range of potential scenarios suggesting a funding gap in 2021-22 of anywhere between £12.8m and £46.8m, with the range of potential outcomes increasing widely beyond 2021-22 (paragraph 41) and that, subject to the inherent uncertainties, the central forecast indicates a potential budget gap of £26.2m in 2021-22.

5. The central budget forecast is based on the assumptions set out at paragraph 23:
  - Additional government funding will be announced to mitigate collection fund deficits as a consequence of the pandemic (50% most likely; 75% best case and 0% worst case);
  - That council revenues will continue to suffer losses in 2021-22 as a consequence of the pandemic and recession;
  - The use of reserves to mitigate resource losses throughout the period 2021-22 to 2023-24 (£5.0m per annum in the most likely scenario, £2.5m best and £10m worst);
  - Council tax will need to increase throughout the period (2.99% per annum assumed);
  - No additional precept for adult social care;
  - Additional costs arising from pay and prices, contractual losses, undeliverable savings proposals and debt financing costs (£20.1m/£14.4m/£24.8m respectively);
  - Debt financing costs arising from additional investment projects (£1.5m in 2021-22 in the most likely scenario);
  - That the Public Health deficit will be written down to support the service as we enter the period of recovery and renewal (£0.9m in the most likely/best case and £1.8m in worst).
6. The funding forecasts contained within this report draw on reserves to mitigate immediate budget pressures; these reserves will need to be replenished in the longer-term;
7. the Strategic Director of Finance and Governance with the support of other Strategic Directors will look to establish medium term budget plans, reviewing any decisions previously taken.
8. Cabinet receive further reports in the autumn as further funding information becomes available and as budget plans for 2021-22 to 2023-24 develop.

## **BACKGROUND AND PURPOSE**

9. Each year, the council updates a detailed Policy and Resources Strategy covering a period that normally reflects the duration of the government's financial settlement. As part of the Policy and Resources Strategy, and in line with requirements of the local government finance act, budgets are approved by Council Assembly for the next financial year as part of Council Tax setting. Where the settlement provides provisional funding commitments for more than one year, budgets may be agreed indicatively for a longer period.
10. For many years this process has formed the pivotal component of the council's financial planning process. This strategy, and the formal approval by council assembly, sits at the heart of the council's commitment to financial planning and efficiency. Most importantly, the strategy is bound to the policies of the council and not least by the commitments in the Fairer Future council plan.
11. In September 2015, the council adopted the Fairer Future Budget Principles that confirmed the framework within which the Policy and Resources Strategy is formed. In September 2016 the cabinet approved the Fairer Future Medium Term Financial Strategy (FFMTFS) and Integrated Efficiency Plan noting the relationship to the Council Plan and the new theme to be fit for the future. The FFMTFS was aligned with the four year local government finance settlement announced in February 2016. 2019-20 was the fourth and final year of the four year settlement.
12. Between 2011-12, the first year of the major austerity cuts, and 2019-20, the council lost government funding in cash terms of more than £146m. According to government calculations, lost spending power exceeded £85m during the same period. Neither of these

figures allowed for the real terms impact of price and demand pressures. In addition, the council has committed to priorities that have needed to be funded through a limited number of sources. During this period the council has also looked to keep council tax as low as possible, protecting the most vulnerable. Southwark remains the eighth lowest council tax rate in London.

13. The 2018-19 local government finance settlement confirmed that London Councils would pilot arrangement for the retention of 100% business rate growth through pooling. The pooling arrangements continued in 2019-20 and 2020-21, albeit on a less generous retention basis (75% in 2019-20 and 67% in 2020-21) and with more risk passed to councils.
14. The Council Plan for the period to 2022 is the council's overarching business plan. The Council Plan contains a range of promises and commitments which the council has worked towards since 2018. These plans will now need to be reviewed in the context of the Covid-19 pandemic. A new plan is intended to be considered by the Cabinet in the autumn.
15. Council Assembly of 26 February 2020 approved a balanced budget and council tax for 2020-21. This was a one year budget due to the uncertainty around future funding.
16. At the beginning of March 2020, the UK and London saw significant uplift in the number of reported cases of individuals with or self-isolating due to showing symptoms of Covid-19, or Coronavirus. A pandemic was well underway with London at the sharp end. In response the council has had to put considerable resources into services. The economic impact has been profound with substantial losses across many of the councils income streams and planned savings delayed or deferred.
17. This report notes the current position with regard to the funding position for the Council and initiates work to update the Fairer Future Medium Term Financial Strategy (FFMTFS) and budget principles.

## **KEY ISSUES FOR CONSIDERATION**

18. This report sets out an initial financial outlook for 2021-22 to 2023-24. This year there is much greater uncertainty than in any previous budget round.
19. At this stage it is extremely difficult to quantify the impact of Covid-19, but the financial pressure on the council will be substantial, even after the Government's emergency Covid-19 funding for local authorities is taken into account. The implications of recession for future council income could be dramatic.
20. The postponement of funding reforms and the absence of government spending plans mean that there is maximum funding uncertainty, making the preparation of medium-term financial plans highly complicated and speculative.
21. The Spending Review which will set out the overall quantum of central government funding to local government was initially intended to be published in the autumn; the Fair Funding Review and new funding baselines within a 75% business rates retention scheme were also planned to be implemented by April 2021. It is highly unlikely that any meaningful funding information or reliable indications of future revenues will now be available before the end of the calendar year.
22. This financial remit report is therefore being compiled in a period of unprecedented financial uncertainty. The report considers the most likely financial position to be faced by the council over the next three years. The forecast however includes a range of assumptions

which may prove to be incorrect; sensitivity testing around these assumptions indicates a significant range of outcomes, as illustrated in the 'fan' chart at paragraph 41.

23. At this stage the 'most-likely' budget scenario is based on the following assumptions:
- That further comprehensive government support will be provided by the government to support local authorities in respect of the pandemic
  - That the councils major revenue income streams (business rates, council tax, fees & charges and commercial income) will continue to be adversely impacted by the Covid-19 pandemic, with modest growth beyond 2021-22
  - Baseline funding will increase in line with inflation
  - the Fair Funding Review and 75% Business Rate Retention will be implemented from April 2022 (with the London Business Rate pooling arrangement continuing)
  - The major grant funding streams, i.e. Public Health Grant, Improved Better Care Fund and Social Care Grants will continue at 2020-21 levels
  - New Homes Bonus scheme will come to an end at 31 March 2021 (with legacy payments only in 2021-22 and 2022-23)
  - Business Rates reset will be postponed to April 2022 (this has not been confirmed but is highly likely). The council is likely to lose £13m as a consequence of the Business Rate Baseline Reset mitigated by the use of reserves set aside for this purpose
  - subject to further analysis, net inflation and pay award pressures of £8.5m have been assumed in the most likely scenario
  - Increased debt financing costs arising from the approved capital programme and potential additional funding for investment projects
  - Lost contractual income and delayed or unachievable savings and income generation
  - Council tax increase throughout the forecast period, with no changes in the local council tax support scheme; no additional adult social care precept has been assumed
  - Retaining the contingency of £4m within the overall budget to support in year cost pressures
  - Write down of the public health deficit as we look to enter a period of recovery and renewal
  - the use of financial risk reserves to mitigate the reduction in available resources (NB in the longer term this use of reserves will need to be replenished).
24. On the basis of the assumptions made at this time, it is estimated that net savings of £26.2m will be required in 2021-22. However the fan chart at paragraph 41 shows a range of potential scenarios which indicate that the actual gap could be between £12.8m and £46.8m.
25. These assumptions will be continually reviewed and updated as firmer information becomes available:

- Funding assistance from Government and Covid-19 funding support;
- Baseline funding level;
- Revenue from locally generated resources – business rates, council tax, fees and charges;
- Inflationary pressures;
- Service and demand led budget pressures, in particular social care services, homelessness, Dedicated Schools Grant and high needs costs;
- Emerging growth and commitments.

26. In the event of further clarity and greater certainty of government funding, we will need to develop our medium term budget plans and review any decisions previously made. Resetting the MTFs and managing risk will require careful attention following the pandemic and as we enter a period of recovery and renewal.

### **COVID-19 Pandemic financial implications**

27. The Covid-19 pandemic is having a considerable impact on the council. The pandemic is hitting our residents, public institutions, businesses and voluntary and community organisations hard. It has required an unprecedented response to mobilise the resources, skills and good faith of many across the borough. We will continue to do all we can to support our residents, communities and local businesses, to keep key services running and ensure that those who need help get it.

28. The outbreak of the Novel Coronavirus (COVID-19), declared by the World Health Organisation as a global pandemic on the 11 March 2020, continues to have significant impacts for council services and major financial implications. The council has had to put considerable additional resources into services to ensure that the most vulnerable in our community are cared for and that the local economy is protected. The economic impact has been profound, and we are expecting substantial losses across many of our income streams.

29. The true scale of the pandemic and its impact on the council's finances will continue to be felt through 2020-21. Significant additional expenditure has been incurred across services with the largest areas of additional spend being within social care, homelessness, hardship support for residents, supporting the voluntary and community sector and support for businesses. The council is also expecting substantial losses across many of its largest sources of income. These include business rates, council tax, housing rents, commercial income, parking, leisure services, regulatory and planning fees.

30. At this stage it is still extremely difficult to quantify the impact of Covid-19, but the financial pressure on the council will be substantial, even after the Government's emergency Covid-19 funding for local authorities is taken into account. The council has sought in recent years to build up its general reserve and financial risk reserves to ensure it is financially resilient. Should the Government not make good on their promise to cover the cost to council's of the pandemic, these reserves will be severely tested and will, in any event, need to be replenished over the coming years.

31. The changing environment in which we are likely to find ourselves as we emerge from 'lockdown' will require the council to review the services it provides. We will need to reset the medium term financial strategy and our capital investment priorities in recognition of the pandemic and any changes to the council's strategic objectives.

32. This report initiates the process for review of the council's medium term financial plan for

the period to 2021-22 to 2023-24, which culminates in budget proposals to Cabinet and Council Assembly for approval in February 2021. The report provides the foundation for the financial planning process and will be firmed up as more certainty.

### **COVID-19 response and next steps into recovery and renewal**

33. At their meetings on 5 May and 16 June, Cabinet received update reports on progress of the #SouthwarkTogether response to COVID-19 and the strategic issues emerging from the ongoing crisis. The reports to Cabinet explained how the COVID-19 response to date has mobilised the resources, skills and good faith of many across the borough to ensure all, especially the most vulnerable, are safe, well and protected. This included taking account of the urgent issues raised in addressing the inequalities exposed by COVID-19, and those articulated by the Black Lives Matter protests, and agreement to take forward a programme of work to respond (the 'Southwark Stands Together' work).
34. Moving forward in the weeks ahead, the council's approach to recovery and renewal will continue to reflect and be shaped by local priorities and needs. It will also need to be guided, where necessary, by national government recovery strategy. On 23 June, the Prime Minister announced that the government would activate the next phase of this strategy ("Plan to Rebuild") from 4 July. This included further easing of lockdown measures and the 're-opening' of wider economic activity and society. It followed the UK's coronavirus alert level moving from 'four' to 'three', meaning the virus is no longer "high or rising" and instead in "general circulation" in the community. In noting this, it's worth remembering that the borough (and country) still remains in the middle of a pandemic, one which continues to test personal, professional and financial resilience for many in our community.
35. Looking more broadly to the months and year ahead, like many places, the borough must be prepared for a potential return to tighter lockdown measures should the virus become more virulent again in our local communities. The system of test and trace which was launched nationally at the end of May is developing and it remains difficult to predict the extent to which this in itself will mitigate wider risks and allow the borough to proceed into a new kind of 'normal'. Future stages of our response are therefore likely to be complex and highly localised. It will require an ability to prepare, plan, respond and adapt at pace to continue to protect those most vulnerable in our community; all whilst continuing to deliver day to day services safely and to the best of our combined ability - and within the resources made available.
36. Further separate reports on individual aspects of the COVID-19 response, and learning to inform the borough's approach to recovery and renewal, will therefore be brought to future Cabinet meetings. This will include consideration of medium to longer term renewal of service plans as part of the refresh of the Council Plan, medium term resources strategy and future budget priorities and plans. An updated Council Plan and financial remit will be presented to Cabinet in September 2020.

### **Local Government funding reform**

37. It remains the Government's intention to implement new funding baselines for all local authorities. The new baselines being based on its review of local needs and resources (the Fair Funding Review), the introduction of 75% business rates retention and resetting business rate baselines. The last time the 'needs based assessment' was updated was for the 2013-14 settlement.
38. However, due to the pandemic, the Government has announced that:
  - the review of relative needs and resource and the introduction of 75% business rates

retention would no longer be implemented in April 2021 as planned

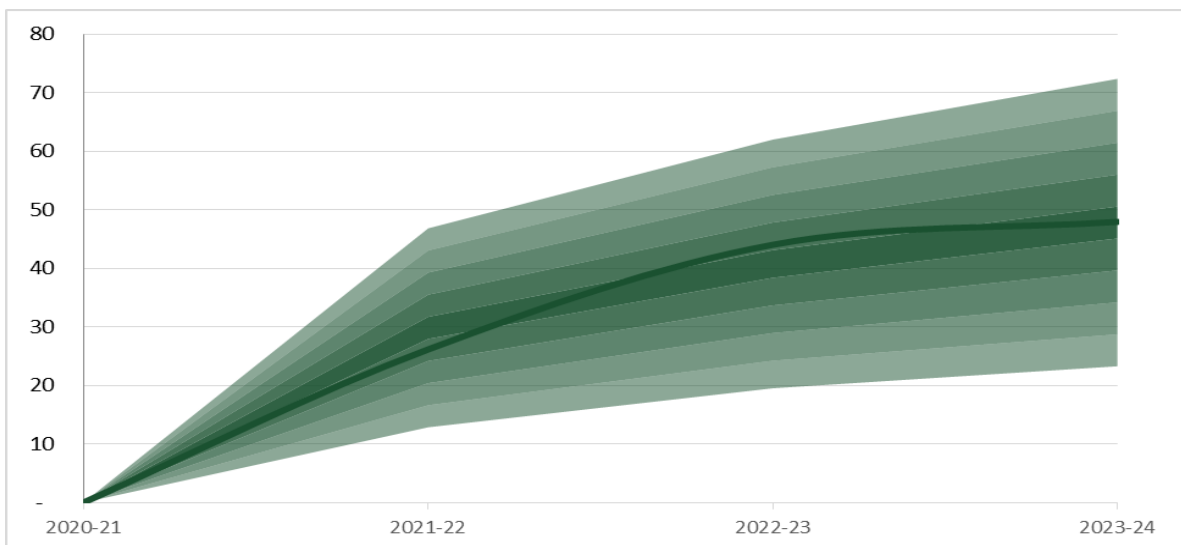
- the revaluation of business rates, due to take place in April 2021, will no longer take place
- the review of business rates will continue and it is assumed this will report back in autumn 2020.

### Spending Review

39. The main strategic funding decisions of central government as they relate to local government are normally made at each Spending Review; although these have been supplemented at subsequent annual Local Government Finance Settlements.
40. The 2019 Spending Review was reduced in scope due to uncertainty over Brexit and covered one-year only (2020-21). It is still unclear whether there will be a Spending Review in 2020 and, if there is, what period it will cover. The absence of any detail about all of the major funding streams creates huge financial uncertainty. Early visibility of local government funding would help local government plan and make effective decisions.

### UPDATED FINANCIAL REMIT 2021-22 – 2023-24

41. This financial remit is being compiled in a period of unprecedented funding uncertainty. The report considers the most likely financial scenario faced by the council over the next three years. The forecast includes a range of assumptions, which may prove to be incorrect; sensitivity testing around these assumptions indicates a range of variations in the financial forecast as indicated in the 'fan' chart below:



42. The solid line represents the 'most-likely' scenario which indicates a gap of £26.2m in 2021-22. However this is within a range of £12.8m (best-case) to £46.8m (worst-case).



43. The 'most-likely' central forecast is illustrated in the table below:

	2020-21 Budget £m	Indicative		
		2021-22 £m	2022-23 £m	2023-24 £m
Settlement Funding Assessment	152.317	155.369	168.499	169.937
BRRS growth	24.739	18.961	0	3.105
Council tax	117.849	118.146	125.255	132.835
Collection fund surplus/(deficit)	(0.612)	(5.532)	(4.500)	(4.500)
Core grants	74.991	68.717	58.500	54.804
Contribution from Reserves	0	5.000	5.000	5.000
<b>Total resources</b>	<b>369.284</b>	<b>360.661</b>	<b>352.755</b>	<b>361.181</b>
Base budget brought forward	354.285	369.284	386.613	396.777
Inflationary pressures	8.486	8.500	8.670	8.844
Commitments and growth	15.223	11.650	3.700	3.500
Efficiencies, income and savings	-8.710	(2.621)	(2.406)	0
<b>Net spending</b>	<b>369.284</b>	<b>386.813</b>	<b>396.777</b>	<b>409.121</b>
<b>Gap (cumulative)</b>	<b>0</b>	<b>26.152</b>	<b>44.022</b>	<b>47.940</b>

## FUNDING FORECAST

44. The main funding sources for the council are:

- Settlement Funding Assessment (comprising retained business rates, a top-up or tariff and Revenue Support Grant);
- Core revenue grants;
- Revenue funding from local taxation (council tax and retained business rate growth);
- Fees and charges.

45. Reliance on locally generated resources has increased significantly since the new funding regime post April 2013. This means the council is far more exposed to the risks arising from income volatility, i.e. business rate growth and losses, council tax income and from fees and charges and commercial income.

46. The pandemic has had major financial consequences for income in 2020-21 and the implication of recession for future council income means the uncertainty of impact is currently at its greatest:

- Income collection rates have been significantly impaired in 2020-21 – is this a deferment, a one-off loss or a continuing trend?
- Reduced tax base growth in 2020-21 – to what extent will this impact in the medium term and what is the speed of recovery?
- Increased council tax support for working age claimants – has this yet reached a peak, when and how long to recover?
- Fees, charges and commercial income – service income has been hit hard by the pandemic, what will be the speed of recovery and impact of post lockdown new normal?

47. The impact on funding reform adds further levels of uncertainty for medium term financial planning.

### Settlement Funding Assessment (SFA)

48. Settlement Funding Assessment (SFA) represents the core funding distributed by the

government. The Relative Needs and Resources formula (Fair Funding Review) and the Spending Review taken together will establish each authority's Baseline Funding Level (BFL). This is the core funding source for authorities and is comprised of retained business rates, business rate top up/tariff and Revenue Support Grant (RSG).

49. The forecast SFA is set out below:

	<b>2020-21 Budget £m</b>	<b>2021-22 Forecast £m</b>	<b>2022-23 Forecast £m</b>	<b>2023-24 Forecast £m</b>
<b>Baseline funding level</b>	152.317	155.369	168.499	169.937

50. For 2020-21 the council was funded via a settlement funding assessment of £152.317m. The central case assumes:

- Core funding will increase annually in line with CPI inflation
- That following the business rate rest in 2022-23, baseline funding will increase in line with national business rate growth achieved since 2013.

### **Revenue Funding from Local Taxation**

51. Local government finance is increasingly dependent on locally generated resources, principally council tax and business rates but also income from fees and charges and income from investment property. Whilst this provides opportunities, it also exposes councils to significant risk in terms of delivering growth and volatility year-to-year, for example exposure to loss of income from business rates appeals.

52. The table below summarises anticipated funding raised through business rate retention and council tax.

<b>Local Resources</b>	<b>2020-21 Budget £m</b>	<b>2021-22 Forecast £m</b>	<b>2022-23 Forecast £m</b>	<b>2023-24 Forecast £m</b>
Business rates retained growth	24.739	18.961	0	3.105
Council Tax – baseline	110.532	117.849	118.146	125.255
Council Tax – growth in tax base	2.795	(3.133)	3.473	3.723
Council tax increase	4.522	3.430	3.636	3.856
<b>Total revenue from local taxation</b>	<b>142.588</b>	<b>137.107</b>	<b>125.255</b>	<b>135.939</b>

### Business Rate Retention

53. In addition to the retained business rate assumptions given by the government, authorities are able to generate additional resources through growth in the rateable value of business premises, above the reset baseline.

54. In the most likely scenario, it is forecast that business rate income will be 6% lower in 2021-22, with modest recovery in subsequent years.

55. The government has confirmed that 75% BRR arrangements will not now be implemented from April 2021 as intended. The forecast assumes the reforms and the business rates

reset will be implemented from 2022-23. This has not been confirmed.

### Council Tax

56. Council tax income for 2020-21 is £117.849m including a council tax increase of 3.99%. Council tax base has grown by over 20% since 2016-17 due to an increase in the number of homes, reduction in the cost of local council tax support and changes to the council tax on long-term empty properties.
57. In reviewing council tax income forecasts, major factors for consideration are:
- Revising growth forecasts assumed for 2020-21 in light of Covid-19
  - Increased take up of working age council tax support. This is likely to be a significant factor in council tax income losses. Claimant numbers have increased significantly and it is likely that numbers will continue to grow over the coming months. Further work will need to be undertaken to model the impact and forecast how quickly the numbers will reduce
  - Impact on collection rates. Council tax collection has been significantly impaired in the first few months of 2020-21. The extent to which these losses are recoverable and any longer term effect on collection rates remains to be seen.
  - The pandemic and a recession will likely necessitate increased bad debt provisions and write-offs.

These factors will need careful scrutiny and review over the coming months.

58. In the context of the serious strains on council funding and the government assessment of individual authorities spending power (which assumes councils will increase council tax each year in line with referendum principles) for planning purposes an assumption of 2.99% council tax increases per annum has been assumed in all scenarios.

### Adult Social Care Precept

59. Since 2016-17 councils responsible for social care have been given the power to raise a social care precept. A 2% ASC precept was applied in 2016-17 and 3% in 2017-18 and 2018-19, and 2% in 2020-21 in order to continue to protect services for our most vulnerable residents. The additional funds bring the total value of the Adult Social Care precept to over £10m per annum.
60. The long awaited government proposals for the sustainable long-term funding of adult social care services has still not been published and it is unclear whether the government's solution to the longer term funding of social care will include additional ASC precepts. No additional precepts have been assumed.

### **Collection Fund surpluses and deficits**

61. The pandemic has seriously impacted on business rate and council tax income in 2020-21. Any deficit on the collection fund in 2020-21 would normally be a charge to the budget in 2021-22 and 2022-23. Subject to new regulations, it has been announced that councils will be able to recover collection fund deficits over three financial years.

### **London Business Rates Pooling Pilot**

62. The council joined the London Business Rate Pool pilot arrangements for financial years 2018-19, 2019-20 and 2020-21.

63. The financial benefit of the pooling arrangement meant that 100% of business rate growth in 2018-19 and 75% of growth in 2019-20 was retained within London. The 2020-21 pooling arrangement was based on 67%. The council has received a share of the pool benefits (one-off resources in 2018-19 and 2019-20) for investment in initiatives set out in the February 2020 budget report. For 2020-21 the pool income will be significantly impaired by the Covid-19 impact and the impact on individual authorities is currently unquantified.
64. No decisions have been made on the continuation of the pool beyond 2020-21.

### Core Grants

65. In addition to baseline funding and revenue funding from local taxation, the Council also receives a number of grants which the government includes in their presentation of local authority core Spending Power.
66. The forecast core grants are set out below:

	2020-21 Budget £m	2021-22 Forecast £m	2022-23 Forecast £m	2023-24 Forecast £m
New Homes Bonus	14.359	7.967	3.697	0
Improved Better Care Fund	17.323	17.323	17.323	17.323
Additional Social Care Grant	10.015	10.015	10.015	10.015
Business Rates Section 31 Grant	5.829	5.946	0	0
<b>Core grant funding</b>	<b>47.526</b>	<b>41.251</b>	<b>31.035</b>	<b>27.338</b>

67. Grants within Core Spending Power:
- New Homes Bonus. New Homes Bonus (NHB) is intended to incentivise housing growth and rewards housing delivery. Nationally £918m was allocated to local authorities in 2020-21 of which Southwark received £14.359m, the third highest reward in the country. The Government has announced that the scheme will not continue its current form and NHB payments in 2021-22 and 2022-23 will be legacy payments for previous growth only. The Government has not consulted on any replacement scheme.
  - Improved Better Care Fund (IBCF). The improved Better Care Fund is made up of two parts, that which was initially included as part of the 2016-17 settlement and the supplementary funding announced as part of the spring 2017 budget. The utilisation of the supplementary grant has been agreed with the Health and Well Being Board for adult social care funding pressures. It is assumed that this funding will continue at the same level.
  - Social Care Support Grant. As part of the autumn 2018 Budget the Chancellor announced additional grant funding for Social Care and winter pressures. This funding has now been combined as the Social Care Support grant and it has been assumed to continue at current level.
  - Section 31 Business Rates compensation grant. The statutory arrangements for business rates retention means that the government must compensate councils for the loss in rate (under Section 31) arising from Government Budget or policy decisions, for example decreases in yield from transitional relief and other discounts. Estimates have been included based on latest returns and any future announcements should be neutral.

This grant would likely end at any business rate reset and be subsumed within updated business rates baselines.

68. Grants outside of Core Spending Power:

- Public Health Grant. Alongside the finance settlement, the government publishes the Public Health allocations. Southwark's allocation for 2020-21 was £27.466m. Prior to 2020-21, Public Health grant had reduced year on year since 2015-16. As part of the move to 75% BRR, Public Health Funding is likely to be incorporated into baseline funding from 2022-23. It has been assumed that this will continue at the same amount as in 2020-21.
- Better Care Funding. The grant is distributed as part of the NHS funding allocation and its use agreed with the Health and Well Being Board. The continuation of the funding was due to be considered as part of the Spending Review. It has been assumed that this will continue at the same amount as in 2020-21.
- Homelessness Reduction Grant. This grant was provided to meet the new burdens costs associated with the additional duties contained within the Homelessness Reduction Act.

### **Fees and charges**

69. The council will seek to generate additional income by reviewing discretionary fees and charges and opportunities to increase other commercial income. In accordance with the councils agreed policy, fees and charges are reviewed annually to increase them to a level that is at least equal to the most appropriate London average, except where this either conflicts with council policy, or would lead to adverse revenue implications or would impact adversely on vulnerable clients. Updated fees and charges will be presented for Cabinet approval in January 2021.
70. Income from fees and charges and commercial rental income have been significantly impacted as a result of the pandemic. In some areas the impact is likely to endure, for example leisure services. The budget forecast makes some assumptions with respect to contractual and commercial income in particular.

### **Cost pressures 2021-22**

#### **Inflation and Pay Costs**

71. The Office of Budget Responsibility forecast that CPI inflation will be around the 2% target. The pay settlement for 2020-21 has yet to be agreed, an assumption of a 2.5% increase to the total pay bill was included in 2020-21. An assumption of 2% per annum has been included for 2021-22 and subsequent years
72. Therefore, this (most-likely) forecast recognises £8.5m of inflationary increases linked to both pay increases and contractual inflation in 2021-22.
73. This ongoing move to self-sufficient local government demonstrates the importance of Southwark's capital investment programme within the borough, either as the lead authority or with partners. Growth is the key to ensuring sustainable budget sources as we move closer to reliance wholly on local taxation, either through business rates or council tax as well as increasing opportunities across the borough for quality of life, jobs and

environmental improvements. This will be particularly challenging as a consequence of the pandemic and the recession.

74. Capital investment is either funded immediately from available capital resources, (e.g. capital receipts or capital grants and contributions) or financed from borrowing (internal or external borrowing). The cost of servicing that debt is charged to the revenue budget over periods commensurate with the period that the investment provides benefits. The most-likely budget forecast includes an increase in debt financing costs of £4m in 2021-22 arising from the exiting capital spending plans and assumed further spending on investment projects.
75. Other budget pressures recognised in the most-likely budget forecast include allowance for planned savings that are now unlikely to be deliverable and the write down of the Public Health deficit in recognition of the additional costs the service is likely to incur post lockdown.

### **2019-20 outturn**

76. The outturn reports for capital and revenue monitoring were presented to Cabinet in June. The 2019-20 statement of accounts is currently subject to audit and is due to be considered for approval by the Audit, Governance and Standards committee in September.
77. The outturn report, presented a balanced budget after movements to/from reserves despite the emerging costs of the pandemic through March 2020, including the immediate commitment of millions of pounds to ensure emergency hardship support was available to residents, communities and businesses.
78. The underlying cost pressures within this balanced budget include the major cost of the emergency tree recovery plan to address the requirements of health and safety regulations and reduce risks to the public; cost pressures arising from a number of emerging issues with the leisure contract; continuing pressures on homelessness and temporary accommodation where spending again exceeded budgeted resources. The contingency was applied to offset these pressures in 2019-20 with additional resources allocated in setting the 2020-21 budget.
79. Elsewhere the operating environment of the Education service continues to be challenging in the light of inadequate funding for high needs and services more generally. Notably there are pressures flowing from the increased numbers of education, health and care plans and the consequential impact upon Special Educational Need transport. The outturn position for the DSG was a £7.0m in-year deficit, bringing the accumulated deficit position to £18.5m at 31 March 2020. There is now clear recognition at a national level that the quantum of funding is inadequate and this is being challenged robustly by local authorities and representative bodies as well as parents. An increased High Needs settlement for 2020-21, combined with a further transfer from the schools block will go some way towards balancing the in-year position; however the prospect of achieving any reduction in the accumulated deficit of £18.5m is distant. To ensure an appropriate level of support and scrutiny, the DSG remains within the Budget Recovery Board process, in partnership with the Schools Forum.
80. The council was able to increase financial risk reserves in closing the 2019-20 accounts in order to support the financial strategy, including an increase in the Spending Review risk reserve.

## **Risks to delivery**

81. The Policy and Resources Strategy covers a wide range of services and plans of the council. It is natural therefore that circumstances and policies can change and develop over time, and the plan has to be based on broad forecasts for later years where decisions have yet to be taken.
82. The council's current and future financial position is subject to a number of risk management processes, and the financial risks affecting the council are captured in the council's risk assessment including:
  - Impact of Covid-19 pandemic and recovery and renewal
  - Changes in local government funding may compromise future service delivery
  - Changes to the business rate retention scheme and any shortfall in business rate recovery will directly impact the council
  - The substantial commitment within the 10 year capital programme is not matched by resources
  - Due to unprecedented financial pressures, the council's financial balances falls below an acceptable level affecting the council's flexibility
  - Future budgets for the council are not sufficiently robust - especially in light of the pandemic, the current economic climate and future funding changes - resulting in restricted council resource and risk of service failure, increased external scrutiny and reputational damage.
83. All risks are subject to regular review. In addition, financial management and monitoring continues to be undertaken on a risk-based approach, with focus on those budgets which are subject to fluctuating demand.
84. It is recognised that the integrated efficiency plan carries a number of significant risks. Delivery of the annual programme of efficiencies, savings and income targets will be difficult, but failure to implement these will inevitably require the council to consider even more difficult decisions.

## **Macro-economic risks**

85. A world-wide recession following the pandemic in addition to the continued hiatus around Brexit and the end of the transition period.

## **Demographic Pressures**

86. The council faces demographic growth pressures and changes in the population profiles which results in both additional numbers of referrals and increased levels of need.
87. Temporary Accommodation and No Recourse to Public Funds are demand driven and have become an increasing pressure on council resources. Caseload remains high with a current upward demand trend.
88. Public Health pressures particularly in sexual health services
89. High-needs cost pressures with rising costs in placements and related transport, increasing demand in services for young people over 16 years old

90. The level of balances remains subject to the scrutiny of the section 151 officer who must ensure that any one off contributions to the budget are appropriate and affordable.

### Reserves

91. As at 31 March 2020 the council had unallocated general fund reserves of £21.002m and net earmarked reserves of £128.449m, including negative reserves for DSG high needs and public health.

92. The net earmarked reserves are maintained to fund:

- invest to save opportunities, which, for example, form part of the modernisation agenda and are expected in part to deliver future ongoing net revenue savings;
- investment in regeneration and development where spend may be subject to unpredictable market and other factors;
- exceptional items or pressures which are difficult to predict and which are not included in revenue budgets or within the capital programme.

Any application of these reserves for budget pressures will necessitate reductions in the programmes of work to be funded from them.

93. General Fund balances may be available in the short term to support the costs of the pandemic but use of these reserves will compromise financial resilience and will need to be maintained at existing levels over the MTFs period. Currently this period is constrained by the level of uncertainty created by lack of information on government funding sources. These remain critical to the council's policy and resources strategy. In recent years this strategy has necessarily been restricted to one year periods. Any use of General Fund balances by implication compromises the budget setting process for future years.

94. The council retains a level of earmarked reserves and these are reported each year within the annual statement of accounts. Reserves play a crucial role in good public financial management. They exist so that the council can invest in service transformation for the future or else allow them to respond to unexpected events or emerging needs. Excluding capital and technical sums such as insurance, usable revenue reserves amount to only a fraction of the council's turnover.

95. The following table summarises earmarked reserves as at 31 March 2020:

<b>Summary of earmarked reserves</b>	Balance at 31 March 2020 £000
<b><i>Reserves committed to specific programmed expenditure and therefore unavailable for unforeseen circumstances:</i></b>	
• Corporate projects and priorities (including Covid-19 funding)	19,541
• Service reviews and improvements	19,350
• Capital programme and other capital investment	23,247
<b><i>Reserves set aside to offset specific liabilities, e.g. DSG, business rate reset, business rate pooling, insurance, PFI whole life costs</i></b>	42,094
<b><i>Reserves set aside to mitigate financial risks which may be available in the short-term but will need to be replenished over time</i></b>	24,317



<b>Summary of earmarked reserves</b>	Balance at 31 March 2020 £000
<b>Total</b>	<b>128,449</b>

96. The legal requirement that a revenue budget deficit is not permissible when it cannot be covered by revenue reserves, applies to any future financial year and not the just the current year. Reserves are one-off resources, they can only be spent once, while service demands will continue year on year.
97. The budget scenarios assume the use of financial risk reserves over the MTFs period. However, the levels of reserves were not designed for the level of volatility arising from the pandemic. Any reserves applied will need to be replenished over future years

### Next Steps

98. The main governance steps to establishing the 2021-22 general fund revenue budget are outlined in the table below:

Date	Meeting	Report	Purpose
September 2020	Cabinet	P&R strategy	Update the financial remit and confirm the size of the budget challenges facing the council in the period to 2021-22 to 2023-24
September - November 2020	<b>Budget Challenge arrangements</b>		
October 2020	Cabinet	P&R strategy	To provide an update including details of Government Spending Review.
November 2020	Cabinet	P&R strategy	To provide an update (if necessary) to include details of any government funding announcements
December 2020	<b>Provisional local government finance settlement</b>		
December 2020	Cabinet	P&R strategy	Provide options for meeting the budget challenges over the next three financial years
December 2020	Cabinet	Council Tax base	Confirm the council tax base to apply for 2021-22
January 2021	Cabinet	P&R strategy	Select proposed solutions for meeting the budget challenge
January 2021	Overview and Scrutiny	P&R strategy	Comment on and make recommendations in respect of the cabinet's proposed 2020-21 budget and indicative budgets for future years
February 2021	Cabinet	P&R strategy	Recommend to Council Assembly balanced budget for 2021-22
February 2021	Council Assembly	P&R strategy	Council Tax setting and approve a balanced budget for 2021-22 and agree indicative budgets for 2022-23 and 2023-24

### Community impact statement

99. The council works in accordance with the single public sector equality duty contained within section 149 of the Equality Act 2010. This means the council must have due regard to the

need to eliminate unlawful discrimination, harassment and victimisation, and advance equality of opportunity and foster good relations between different groups.

100. Transparency and fairness form part of the seven budget principles and are an underlying principle in the Council Plan. As with the budget for 2020-21 and for previous years, each department will undertake equality analysis/screening on its budget proposals ahead of the final decisions being taken. Where screenings identify potential impacts, more detailed analysis is being carried out.
101. Undertaking equality analysis helps the council to understand the potential effects that the budget proposals may have on different groups. The analysis also considers if there may be any unintended consequences and how any of these issues can be mitigated. Analysis is also undertaken to consider any crosscutting and organisation-wide impacts.
102. For many services the budget proposals will include efficiencies which have staffing implications. As specific proposals are brought forward, and at each stage of implementation thereafter, the different impacts on different categories of staff will be assessed in accordance with the council's reorganisation, redeployment and redundancy procedures.
103. Equality analysis will continue through the cycle of planning and implementation of these budget proposals. In line with our Public Sector Equality Duty, any changes to services arising from these proposals will be implemented in such a way to not impact disproportionately on any specific section or group in our community. Where necessary, consultation will be undertaken alongside mitigating actions where necessary. In line with the process across the council, information on the equality analysis will be shared with the relevant cabinet members so it can be considered when decisions are taken. The equality analyses will be collated across the council to look for any cumulative impacts.
104. To date no cumulative impacts have been identified through the analysis. However, this process will be completed in time to be reported on in the final budget report in January 2021.

## **SUPPLEMENTARY ADVICE FROM OTHER OFFICERS**

### **Director of Law and Democracy**

105. The constitution determines that cabinet consider decisions regarding the strategic aspects of the regulation and control of the council's finances. The council has a legal obligation to set a balanced budget on an annual basis as prescribed in the Local Government and Finance Act 1992 and associated Regulations. The issues contained in this report will assist in the future discharge of that obligation.
106. The council is required under section 149 of the Equality Act 2010 to have due regard to the need to:
  - Eliminate unlawful discrimination harassment and victimisation
  - Advance equality of opportunity between people who share protected characteristics and those who do not
  - Foster good relations between people who share protected characteristics and those who do not.
107. Decision makers must understand the effect of policies, practices and decisions on people with protected characteristics.

108. Equality analysis is the mechanism by which the council considers these effects. The report sets out how it is proposed equality analysis will be undertaken in relation to the budget proposals.

109. It is essential that cabinet give due regard to the council's duty under the Equality Act 2010 and the implications for protected groups in the context of that duty in relation to this decision and future decisions on the budget proposals.

#### **REASONS FOR URGENCY**

110. Each year, the council updates a detailed Policy and Resources Strategy covering, as a minimum, the following financial year. This report initiates the 2021-22 to 2023-24 budget planning process and the detailed work on budget proposals. Members and officers will undertake this work over the coming months in order to meet the timetable to prepare a budget proposal for submission to council assembly in February 2021.

#### **REASONS FOR LATENESS**

111. The Chancellor of the Exchequer presented a mini-budget on Wednesday 8 July 2020. We continue to await announcements from the government on further financial support to help meet the costs of the council's response to the pandemic in addition to indications of funding for 2021-22 and future financial years. The lack of clarity makes the preparation of financial plans a highly speculative task.

#### **BACKGROUND DOCUMENTS**

<b>Background Papers</b>	<b>Held At</b>	<b>Contact</b>
Policy and resources strategy 2020-21 – revenue budget	160 Tooley Street London SE1 2QH	Rob Woollatt 020 7525 0614
<b>Link:</b> <a href="https://moderngov.southwark.gov.uk/documents/s89256/Report%202019-20%20outturn%20revenue.pdf">https://moderngov.southwark.gov.uk/documents/s89256/Report%202019-20%20outturn%20revenue.pdf</a>		

#### **APPENDICES**

<b>No:</b>	<b>Title</b>
None	

## AUDIT TRAIL

<b>Cabinet member</b>	Councillor Victoria Mills, Finance, Performance and Brexit	
<b>Lead officer</b>	Duncan Whitfield, Strategic Director of Finance and Governance	
<b>Report author</b>	Rob Woollatt, Interim Departmental Finance Manager	
<b>Version</b>	Final	
<b>Dated</b>	9 July 2020	
<b>Key Decision?</b>	Yes	
<b>CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / CABINET MEMBER</b>		
<b>Officer Title</b>	<b>Comments Sought</b>	<b>Comments included</b>
Director of Law and Democracy	Yes	Yes
Strategic Director of Finance and Governance	Yes	Yes
Cabinet Member	Yes	Yes
<b>Date final report sent to constitutional team</b>		10 July 2020