

SCRUTINY COMMISSION – 4 NOVEMBER 2015

REVIEW OF EARMARKED FUNDS AND BALANCES

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

Purpose of Report

1. To report the findings of a detailed review of revenue earmarked funds.

Policy Framework and Previous Decisions

2. The earmarked funds strategy was approved by the County Council at its budget meeting on 18 February 2015 as part of the Medium Term Financial Strategy (MTFS). Earmarked funds are reviewed three times during the financial year.

Review of Earmarked Funds

3. The review covered all revenue earmarked funds excluding schools. The main elements were to:
 - a) review if earmarked funds were required and the appropriate level;
 - b) review the spending and contribution profiles for the main earmarked funds over the next four years;
 - c) review the appropriate level of the General County Fund;
 - d) reallocate balances as required.

Earmarked Funds

4. Earmarked funds are held in accordance with the County Council's Earmarked Funds Policy that is approved annually by County Council as part of the MTFS – a copy is attached as Appendix A.
5. The level of earmarked funds excluding schools and partnerships was £90.2m as at 31 March 2015, see Appendix B for details. The opening balances have been reviewed and updated as part of the review of earmarked funds. These amendments are shown as transfers in Appendix B. The main amendments are:
 - Transformation Fund (£3m) – transfer to the Capital Financing earmarked fund to fund additional expenditure items approved by Cabinet on 11th September 2015;
 - The Housing Related Support earmarked fund (£0.5m) has been consolidated into the Adults and Communities Developments fund, as the

purpose of the funds was identical: supporting departmental transformation;

- A transfer has been made from the Adults and Communities Developments fund to the Adults and Communities Renewal of Equipment and Vehicles earmarked fund (£0.2m);
 - Transfers of elements of earmarked funds which are no longer required for their original purposes to the Transformation Fund (£0.1m).
6. Following the review of earmarked funds, the updated list of earmarked funds and forecast of balances for the next four years are detailed in Appendix C.
 7. The following paragraphs consider each earmarked fund in detail and show a projection of the balances at 31 March 2016.

Renewals of Equipment and Vehicles (£4.3m)

8. Departments hold earmarked funds to provide funds for the future replacement of vehicles (the County Council has a fleet of around 500 vehicles) and equipment such as ICT.
9. The earmarked funds are;
 - Children and Family Services (£1.9m). This earmarked fund has been established to respond to the need to develop, improve and where necessary replace departmental management information systems such as Capita One and Frameworki;
 - Adults and Communities (£0.7m). This provides funding for the future replacement of equipment, vehicles and departmental IT systems;
 - Environment and Transport (£0.2m). This is mainly used to fund replacement of vehicles and equipment, both those used for Highway Maintenance activity and also those used within the Passenger Fleet team for School and Social Care Transport;
 - Corporate Resources (£1.5m). This will be used to fund renewal of the County Council's ICT infrastructure. The balance on the fund will be maintained to manage higher than average demand in individual years and to save for future planned upgrades.

Trading Accounts (£0.5m)

10. Surpluses from the Industrial Properties trading account are transferred to an earmarked fund to provide funds for future capital investment, large maintenance items and to smooth volatility in revenue performance.

Insurance (£17.7m)

11. Earmarked funds of £10.2m are held to meet the estimated cost of the insurance policy excesses that the Council is liable for. This is for historic incidents that have not yet been reported to the Council and an amount to allow excesses of large property claims to be met. This enables the Council to meet excesses regardless of the timing of claims, which can be erratic. The levels are assessed periodically through an Actuarial Review. The next review is planned for the end of 2015/16. Excesses include:
 - Property damage (including fire) £500,000;
 - Public / Employers' liability £250,000;
 - Professional indemnity £25,000;
 - Fidelity guarantee £100,000;
 - Money – completely self-insured.
12. Schools schemes and risk management (£0.4m). The County Council arranges contents insurance for schools with an excess of £50,000. To protect schools from large losses the County Council retains a proportion of the saved premiums to pay claims that are above the level of excess that a school would normally expect (£200) up to the insured level (£50,000). A balance is built up in low claim years to allow the cost of high claim years to be met. Similarly a claims contingency is held for the Human Resources advisory scheme, operated by the County Council, for schools, in case of employment disputes resulting in a tribunal. The fund is also used to fund risk management initiatives to try and reduce claims in future years.
13. The uninsured loss fund of £7.0m is required mainly to meet potential liabilities arising from Municipal Mutual Insurance Ltd (MMI) that is subject to a run-off of claims following liquidation in 1992. The fund also covers the period before the Council purchased insurance cover and the period (1993-97) that the Council was insured with Independent Insurance, who have entered provisional liquidation.
14. The MMI run-off is regulated by a scheme of arrangement (the scheme) entered into by the creditors of MMI. The scheme provides for a clawback against the creditors in the event that the assets of MMI at the time of liquidation prove insufficient to meet its liabilities. MMI's 2014/15 accounts show a significantly worsening position due to the estimated costs of future mesothelioma and abuse claims, calculated by MMI's actuaries. It is expected that a future levy payment will be required in 2016/17, and c£2m is reflected in the earmarked fund forecast.

Committed Balances (£1.3m)

15. Two earmarked funds are used as a mechanism to carry forward resources where expenditure has been committed to projects but the expenditure has not been incurred in that financial year. The two earmarked funds are the Central Maintenance Fund (CMF), £1.1m and the earmarked fund for community grants, £0.3m. Due to the on-going nature of maintenance it is expected that there will always be a balance on the CMF fund.

Children and Family Services

16. Supporting Leicestershire Families (£1.9m). This earmarked fund is used to fund the Supporting Leicestershire's Families service which is providing early help and intervention services for vulnerable families across Leicestershire. The majority of this fund is expected to be utilised in 2016/17.
17. Children and Family Services Developments (£2.7m). This general earmarked fund provides funding for a number of projects within the department such as improving management information, information access and retention and responding to changing requirements as a result of OfSTED and legislation. The financial position of the department in 2014/15 allowed costs to be met from the budget rather than the fund.
18. Youth Offending Service (£0.2m). This earmarked fund is used to fund the Youth Offending Service.
19. Special Educational Needs Disability (SEND) (£0.8m). Local authorities have received grant for the implementation of a national redesign of services for children with special educational needs and disabilities. Changes in national expectations and recruitment difficulties have resulted in some elements of implementation being re profiled.

Adults and Communities

20. Adults and Communities Developments (£4.6m). This earmarked fund is held to fund a number of investments in maintaining social care service levels and assisting the department in achieving its transformation. Due to the expected reduction in Care Act funding, following the reduction in scope, underspends arising in the current financial year relating to this activity are being held in the fund to manage a smooth transition. Hence the fund is expected to have a net increase in the current financial year.
21. Health and Social Care (£5.0m). Approximately half of this earmarked fund is used to fund projects that improve health and social care outcomes in Leicestershire, including the prevention of admission and readmission into hospital as well as the prevention of other costly health and social care provision. Funding for these projects has been aligned with the strategic objectives of the Better Care Fund (BCF) and has been agreed between the County Council and partners from the NHS. The other half of the fund has been set aside as a contingency for underperformance against future pay for performance BCF metrics.
22. Museums and Arts (£0.0m). This earmarked fund represented the income received from the sale of artefacts. The fund is being used to maintain the quality of existing collections and is expected to be fully utilised in 2015/16.
23. Adults and Communities Extra Care (£0.9m). This earmarked fund was created from elements of the New Homes Bonus grant that were ring fenced by the Cabinet for Extra Care schemes. There is a scheme currently in development in

Charnwood (£0.3m). Further opportunities will be investigated following the refresh of the Extra Care strategy.

Public Health

24. Public Health (£1.6m). The NHS grant for Public Health was above the level of historic expenditure, recognising the historic underfunding in Leicestershire. This will be used for preventative and other Public Health beneficial activities.

Environment and Transport

25. Commuted sums (£2.2m). This is used to cover future revenue costs arising from developer schemes, where the specifications are over and above standard developments (e.g. block paving, bollards or trees adjacent to the highway). These liabilities can arise many years after the funding is received and as such a link is not always made between work undertaken at these developments and the contributions received, and therefore the balance on this earmarked fund has built up over time. The intention is to utilise the resources over the next few years (£0.4m per year) to help mitigate against the impact of the overall reductions in resources available for highways maintenance, although it is likely that additional amounts (£0.2m per year) will be received which will increase the fund balance over this period.
26. Civil Parking Enforcement (£0.1m). This is a small earmarked fund that is held on behalf of the District and County Partnership which is responsible for the enforcement of on and off street parking in Leicestershire. It will be utilised for equipment and technology replacement in future years.
27. Waste Infrastructure (£0.3m). This is available to fund general improvements to the Recycling and Household Waste Sites (RHWS), the remaining costs of the Waste Transfer Station (WTS) at Whetstone and a new transfer station at Coalville. By the end of the 2016/17 financial year it is expected that this fund will have been utilised.
28. Section 38 Income (£0.5m). This is income received from Housing Developers paid in advance and used to cover County Council costs for design checking, on site inspection of works during construction and administration of the process to ensure newly built estate roads are to the required standard for adoption. The signing of the final certificate to agree new roads are at the required level should be carried out within a 4-year period. Section 38 income is paid into the earmarked fund and brought into the accounts to offset the costs in the year in which they are incurred. The majority of the current fund balance will be utilised over the next four years. However, it should be noted that additional funding may become due and be received over this period which would increase the balance on this fund.
29. Section 106 Income (£0.5m). Funding received to meet developer-related revenue expenditure (such as subsidised bus services and travel packs linked to new developments) and where there are no specific conditions for the funding to be repaid. The majority of the current fund balance will be utilised over the next four

years. However, it should be noted that additional funding may become due and be received over this period which would increase the balance on this fund.

30. Leicester and Leicestershire Integrated Transport Model (LLITM) (£0.2m). This is money identified to update the LLITM to ensure it accurately predicts the impact of future prospective developments and supports potential bids for future major schemes. This is expected to be spent by 2017.
31. Capital Major Projects - advanced design (£0.4m). This earmarked fund will be used to fund feasibility studies and advance design works to enable bids to be made for major capital schemes to improve the transport infrastructure supporting expected growth in Leicestershire.
32. Other earmarked funds (£0.1m). These funds will be used for partnership transport projects.

Chief Executive's

33. Community Planning (£0.2m). This funding is held to support a range of various initiatives with partners and communities within Leicestershire including support for affordable rural housing for older people.
34. Economic Development (£0.9m). This earmarked fund was established to provide funding for economic development proposals. These proposals are contained in the Enabling Growth Plan that is currently in draft form.
35. Leicestershire Local Enterprise Fund (£1m). This earmarked fund was established to provide funding for a business loan scheme which will provide a gradual return of funding to the County Council, unless it is reinvested. At 31 March 2015 a total of £0.3m in loans had been made.
36. Legal (£0.3m). This earmarked fund is held to provide funding for temporary solicitor posts to cope with the current and transformational demand.
37. Signposting and Community Support Service (£0.8m). This fund was established to mitigate the impact of the withdrawal of Government funding for the Leicestershire Welfare Provision. The funding was provided from underspends in the scheme's two years of operation (2013/14 and 2014/15) and will be used to temporarily support signposting and community support for vulnerable people, with the aim of minimising the on-going costs of this service over the next four years.
38. Other (£0.6m). This earmarked fund holds funding towards a variety of projects and contingencies. The projects are phased over several years and include; efficiency projects, planning control work, and funding received from (and ring fenced to) crime fighting and prevention.

Corporate Resources

39. Corporate Resources Other (£0.7m). The main purpose of this earmarked fund is to provide funding to efficiency projects and one off initiatives in Corporate Resources. Examples of activities funded are investigating asset management changes/improvements and ICT development work. Funding is also held on behalf of the Multi Agency Travellers Unit.

Corporate

40. Transformation (£19.5m). The fund is used to invest in transformation projects to achieve efficiency savings and also to fund severance costs. To achieve the level of savings required within the MTFS the Council will need to change significantly and this will require major investment including in some of the core 'building blocks' of transformation such as improvements to data quality and improvements to digital services enabling more self-service.
41. Capital Financing (£18.0m). This fund is used to hold MTFS revenue contributions to fund capital expenditure in future years including the Street Lighting LED replacement project and investment decisions agreed by Cabinet on 11th September 2015 from in year resources. The significant increase in 2015/16 relates to planned contributions from the 2015/16 MTFS for profiled spend on LED in 2016/17 and later years.
42. East Midlands Shared Services – IT developments (£0.5m). Funding set aside for EMSS investment in Oracle development projects to support the shared service.
43. Environmental / Energy Efficiency programme (£0.1m). This funding has been set aside to support various invest to save projects to reduce carbon emissions and generate future revenue savings. The programme has been superseded with the Energy Strategy programme included in the Capital Programme.
44. Elections (£0.6m). The average cost of County Council elections is estimated to be £0.8m every four years, unless there are other elections on the same date that can share the cost. The earmarked fund is built between elections using budgeted annual contributions of £0.2m.
45. Broadband (£2.4m). This fund was established to allow the development of super-fast broadband within Leicestershire. A contract has been entered into with BT and they have commenced work. There is a significant time lag in spending County Council funds due to grant conditions that required Central Government and European funding to be spent within a set period. The majority of the funding is expected to be spent in 2017/18.
46. Loughborough Science Park (£1.1m). This fund was established from a prior year provision for an investment in partnership with Loughborough University and Charnwood Borough Council towards the next phase of development on the Science and Enterprise Park campus.

47. Other (£0.3m). This amount relates to the balance of funding set aside to fund the development of a school place planning strategy to support significantly increased capital funding in 2015-18.
48. Business Rates Retention (£1.0m). This fund has been established following the introduction of the Business Rates Retention system in 2013, as a contingency to fund potential shortfalls in business rates income impacting in later years, especially the risk of large appeals and fluctuations in Business Rates income.
49. Local Authority Mortgage Scheme (LAMS) (£-8.4m). The County Council has invested £8.4m in the Local Authority Mortgage Scheme to make it easier for first time house buyers to obtain mortgages and thus stimulate the local housing market and benefit the wider local economy. Investment of £3m in 2013/14 and £5.4m 2012/13 has been advanced to Lloyds bank, temporarily funded from the overall balance of earmarked funds. The funding will be returned to the County Council, 5 years after the date it was advanced, in 2017/18 and 2018/19.
50. Pooled Property Fund(s) (-£15m). Cabinet on 11 September 2015 approved the investment of £15m of the Council's earmarked funds into a pooled property fund. The Pension Fund property advisor has submitted a recommendation to invest in two UK pooled property funds (£7.5m in each) with Lothbury Property Trust and Hermes Property Unit Trust and this has been agreed by the Lead Member for Corporate Resources. This will raise interest by a significant amount, in effect replacing £15m at 0.5% with £15m at around 4%. There will only be a part-year impact in the current year and the level of impact will depend on the timing of the investment(s), which will depend to a certain extent on market conditions. The investment is funded from the overall balance of earmarked funds and can be realised in the future when required.

Other

51. Potential Health transfers (£5m) – Estimate of year end transfers to the County Council.

Schools / Partnerships Earmarked Funds

52. Dedicated Schools Grant (£6.9m). DSG is ring fenced and can only be applied to meet expenditure properly included in the Schools Budget, as defined in the School and Early Years Finance (England) Regulations. Any underspend on services funded by DSG must be carried forward and ring fenced to those services. This fund is earmarked to fund any deficit budget that reverts back to the local authority as maintained schools move into sponsored academy arrangements and also to meet the revenue costs of commissioning places in new schools. A forecast overspend of £3m in the current year is forecast in the reduction as at 31st March 2016.
53. Leicestershire and Rutland Sport (£0.8m). The earmarked fund's main purpose is to hold partner contributions until expenditure on the agreed activities has been incurred. A significant part of the services funding from external agencies is

uncertain in nature, so the earmarked fund also allows management of funding variations and a redundancy provision.

54. Centre of Excellence (£0.7m). The Centre of Excellence for Information Sharing is a local-national collaboration, funded by multiple government departments. It is hosted by Leicestershire County Council, and has a team of people from across national and local organisations. The organisation's vision is for users of public services to achieve better outcomes as a direct result of improved information sharing between agencies and local places. The earmarked fund is held on behalf of the Centre of Excellence to fund ongoing work.
55. Leicestershire Social Care Development Group (LSCDG) (£0.4m). This earmarked fund is held on behalf of the LSCDG, a partnership with Leicester City Council. Funds are held on behalf of the partnership to meet the Director of Adults and Communities responsibility for workforce development in social care regardless of the sector. The monies are solely for the independent and voluntary sector across the sub region.
56. East Midlands Shared Services – Other (£0.3m). This relates to the County Council's share of the current year forecast underspend, to be used for future EMSS developments.

Other Issues

57. There are real advantages to the County Council of having a strong balance sheet in a period of economic crisis. These are obvious such as a greater ability to weather financial shocks, but there are also advantages such as the ability to use this strength to implement policy decisions such as LAMS and the Leicestershire Local Enterprise Fund that offset, to an extent, the impact of the failure of banks to provide finance.
58. The overall level of earmarked funds includes significant balances for capital financing (£18m at the end of 2015/16) which are required to fund the County Council's Capital Strategy. These resources have been set aside from revenue underspends, surplus earmarked funds and the current MTFs, to avoid the need to undertake external borrowing.
59. Members requested details regarding earmarked funds where the latest projections varied significantly from the previous forecast. Appendix D gives details of earmarked funds where forecasts as at 31st March 2016 have varied by more than £0.5m.
60. Appendix E reproduces an article from The Telegraph on 31 August 2015 which refers to the possibility that the Chancellor may take action in the Spending Review to "force local authorities to lessen the impact of budget cuts by tapping into their huge reserve pots". The results of the Spending Review will be announced on 25th November 2015 and any specific requirements regarding the use of earmarked funds will be taken into account in the preparation of the 2016 MTFs, which will be reported to the Cabinet and the County Council in February 2016.

Schools Earmarked Balances

61. Schools and colleges are allowed to retain their accumulated balances in relation to delegated budgets. Schools balances have reduced from £8.1m in 2013/14 to £7.6m at the end of 2014/15, mainly as a result of academy conversions.

General County Fund

62. The General County Fund is held to meet any unexpected risks. The balance on the General County Fund has increased to £14.8m as at 31st March 2015 from £10.8m as at 31st March 2014 and is expected to remain at £14.8m in 2015/16.
63. The policy on the General County Fund has been to maintain balances in line with the inherent risks faced by the County Council. The required level of earmarked funds is kept under review during the year and a more formal assessment is undertaken at the time the Medium Term Financial Strategy (MTFS) is rolled forward. The policy will be to continue to maintain a level of the General County Fund consistent with the overall financial environment. The level of the General County Fund is currently within the target range of 4 to 5% of net expenditure (excluding schools), the balance of £14.8m represents 4.2% of net expenditure for 2015/16.

Risk Assessment

64. As part of the earmarked funds review, the risk assessment was revisited given the rapidly changing financial environment. This shows that the risks faced by the County Council are increasing. The key risks are set out below:
- Public finances are deteriorating with the prospect of further cuts in funding for the next four years which will increase the County Council's savings requirement;
 - The localisation of business rates and changes to Council Tax Benefit mean that the income of the Council will be less predictable and potentially subject to in year shocks;
 - Environment including extreme weather;
 - Service pressures resulting in overspend. Although overall the Council is underspending, pressures within Adults and Children's social care are increasing. National funding changes could exacerbate these pressures;
 - Potential cuts to grant funding for Public Health;
 - Funding the introduction of the National Living Wage;
 - Increase in demand for SEN transport.

65. The current MTFS includes a contingency in the budget of £8m over the four years of the MTFS. This needs to be considered alongside the General County Fund in relation to the risks faced by the County Council.

External Audit Review

66. PricewaterhouseCoopers (PWC), our external auditors, have reviewed the 2015/16 – 2018/19 MTFS. This was reported to the Corporate Governance Committee on 12th June 2015. This review covered a number of aspects including earmarked funds and contingencies. The review showed that the uncommitted General County Fund balance of £14.8m, which represents 4.2% of net spend, is relatively low when compared to other authorities, but the gap is smaller than in previous years. The policies in the benchmark group ranged between 2% and around 7% of net spend. PWC stated “Your policy is within our expectation for the level of general fund reserves which we would independently expect you to hold”.
67. However, PWC commented that earmarked funds of £84.7m (excluding schools) at 24% of net spend were higher than the average data collected of around 16%. PWC noted that “These are being held to manage the transition period, fund specific cost pressures and to deliver the transformation programme which you have set out in your MTFS. The costs associated with this transformation, such as severance costs, are being met through the use of these reserves rather than recurrent spending.”
68. PWC concluded by stating, “You have set aside a prudent level of earmarked reserves and contingency to manage future cost pressures. Whilst these are larger than in other similar Local Authorities, we believe that you have a prudent approach in setting your MTFS. These reserves will be required to effectively deliver the transformation you require.”

Management and Monitoring of Earmarked Funds

69. At present information on earmarked funds is provided in the following reports;
- February – MTFS reports to the Cabinet and County Council. These reports contain the earmarked funds policy, forecast levels of funds and statement on the robustness of estimates, risks and funds.
 - June/July – Outturn report to the Cabinet and Scrutiny Commission. These reports contain the key movements and the actual year end balances.
 - September – Statement of Accounts report to Constitution Committee. This report sets out the earmarked funds in detail and includes a commentary and a statement showing all the transfers to and from the earmarked funds.
 - Autumn review of earmarked funds to Cabinet and Scrutiny Commission.

Conclusions

70. The review of earmarked funds has identified that:

- £0.1m of earmarked funds are no longer required and these have been released to the Transformation fund (see Appendix B);
- At the time of agreeing the MTFs further information will be available that could mean further earmarked funds will be released;
- That the level of earmarked funds (excluding Dedicated Schools Grant and partnerships) is expected to fall to £74.8m by the end of 2015/16.

Recommendations

71. Members are asked to note the findings of this review.

Background Papers

None.

Circulation under Local Issues Alert Procedure

None.

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List of Appendices

Appendix A – Earmarked Funds Policy

Appendix B – Earmarked Funds Restated

Appendix C – Earmarked Funds Projection

Appendix D – Earmarked Funds where balance projected at 31/3/16 has varied by more than £0.5m

Appendix E – Article from The Telegraph 31 August 2015

Equality and Human Rights Implications

There are no direct implications arising from this report.