Leicestershire County Council

SCRUTINY COMMISSION – 31ST JANUARY 2022

PROVISIONAL MEDIUM TERM FINANCIAL STRATEGY 2022/23 - 2025/26

REPORT OF THE DIRECTOR OF CORPORATE RESOURCES

Purpose of the Report

1. The purpose of this report is to:

   a) Provide information on the proposed 2022/23 to 2025/26 Medium Term Financial Strategy (MTFS) as it relates to Corporate and Central Items;

   b) Provide an update on changes to funding and other issues, arising since the publication of the draft MTFS;

   c) Provide details of the following strategies and policies: Earmarked Funds Policy, Capital Strategy and the Corporate Asset Investment Fund Strategy;

   d) Ask members of the Commission to consider any issues as part of the consultation process and make any recommendations to the Cabinet accordingly.

Timetable for Decisions (including Scrutiny)

2. On 14th December 2021 the Cabinet agreed the proposed MTFS, including the 2022/23 revenue budget and 2022/23 to 2025/26 capital programme, for consultation. The Overview and Scrutiny Committees and the Scrutiny Commission will consider the proposals during January 2022.

3. An update of the MTFS will be reported to the Cabinet on 11th February 2022, and then to the County Council on 23rd February 2022 to approve the MTFS including the 2022/23 revenue budget and capital programme. This will enable the 2022/23 budget to be set before the statutory deadline of the end of February 2022.

Policy Framework and Previous Decisions

4. The MTFS is a rolling financial plan that is updated annually. The current MTFS was approved by the County Council on 17th February 2021. The County Council's Strategic Plan (agreed by the Council on 6 December 2017) outlines the Council's long-term vision for the organisation and the people and place of Leicestershire. The MTFS, along with other plans and strategies such as the Transformation Programme, aligns with and underpins the Strategic Plan.

MTFS Summary – Cabinet 14th December 2021

5. The draft MTFS was approved by the Cabinet on 14th December 2021.

6. The key revenue budget details were:

   - One year Local Government Settlement
   - No Revenue Support Grant
   - Council Tax increase of 1.99% plus 1% Adult Social Care Precept in 2022/23, and 1.99% for the following three years
   - Growth of £88m is required, primarily to meet the forecast increase in demand for social care
   - Provision for pay and price inflation, £69m, driven by the National Living Wage (NLW) and relatively high inflation forecasts for 2022/23
   - Savings required of £100m - of which £40m are identified, £14m relate to Special Education Needs, leaving a shortfall of £46m to be found.

7. The key capital programme details were:

   - The draft four-year capital programme totals £514m
   - Capital funding available totals £363m
   - Balance of £161m, temporarily funded from the County Council's internal cash balances in advance of section 106 contributions and other funding being received in the future, e.g. increased capital receipts or new grants.

Changes to the Revenue Budget 2022-26

8. A summary of the overall MTFS revenue position as reported to Cabinet on 14th December 2021 is shown in Appendix A.

9. Since the report to the Cabinet, the Local Government Settlement was announced. Changes from the settlement and other known issues since then are summarised below.

	2022/23 £m	2023/24 £m	2024/25 £m	2025/26 £m
Shortfall at 14th December 2021	0.0	11.5	29.0	46.4
Funding changes				
Business Rates Section 31 Grant	-1.3	-1.3	-1.3	-1.3
New Homes Bonus Grant	-1.2	0.0	0.0	0.0
Improved Better Care Grant	-0.5	-0.5	-0.5	-0.5
Social Care Grant	-5.7	-5.7	-5.7	-5.7
Services Grant (2022/23)	-4.3	0.0	0.0	0.0
New Grant (assumed share of £1.6bn - replaced)	8.0	8.0	8.0	8.0
Market Sustainability & Fair Cost of Care	-1.6	-1.6	-1.6	-1.6
Council Tax Precept	0.6	0.6	0.6	0.6
Council Tax Collection Funds	-2.0	0.0	0.0	0.0
Provision for impact of Covid-19 on funding	-1.0	-1.0	-1.0	-1.0
Budget Equalisation Earmarked Fund – contribution changes	7.4	-5.7	-7.1	-8.3
Other Changes				
Inflation Contingency	1.6	3.6	3.6	3.6
Other	0.0	0.0	-0.2	-0.8
Revised Shortfalls	**0.0**	**7.9**	**23.8**	**39.4**

10. Business Rates Section 31 Grant – the provisional Settlement includes section 31 grants reflecting CPI inflation, whereas the final Settlement will be updated to reflect RPI inflation levels, which will increase income to the Council by around £1.3m.

11. New Homes Bonus (+£1.2m) updated estimate per the 2022/23 Local Government Finance Settlement. The Settlement includes an additional year of the grant and the remaining legacy amount of £0.9m, in respect of 2019/20, both of which will be phased out by 2023/24.

12. Improved Better Care Fund (+0.5m) updated estimate per the 2022/23 Settlement.

13. Social Care Grant (+£5.6m) increased allocation in the Settlement. The allocation includes an adjustment based on the relative levels of funding that Councils can raise from council tax (via the Adult Social Care Precept), which reallocates grant from areas such as County Councils to areas with low council tax levels, particularly in London. This is causing the County Councils share of the national allocation to reduce each year.

14. Services Grant 2022/23 (+£4.3m). The Settlement includes a one-off grant of £822m nationally, of which the County Council will receive £4.3m. The Settlement states that “This will provide funding to all tiers of local government in recognition of the vital services, including social care, delivered at every level of local government. This grant includes funding for local government costs for the

increase in employer National Insurance Contributions" and also that the Government "intends to work closely with local government on how to best use this funding from 2023/24 onwards".

15. New Grant 2022/23 (-£8.0m). The draft MTFS included an estimate that the County Council would receive around 0.5% of the additional funding referred to in the Chancellor's Spending Review. That assumption can now be removed and be replaced by the grants announced in the Settlement.

16. Market Sustainability and Fair Cost of Care Fund (+£1.6m). The Settlement includes £162m for this new ringfenced funding, of which the County Council will receive £1.63m. The funding is towards the inflationary and demographic pressures facing adults and children's social care services. The central inflation contingency will be increased by £1.6m to reflect this additional funding.

17. Council tax precept 2022/23 tax bases provided by the District Councils are 0.2% lower than previously anticipated, leading to a £0.6m reduction in income. This is offset by the removal of a £1m provision included in the draft MTFS for the impact of Covid-19 on income levels.

18. Provisional council tax collection fund estimates for 2021/22 have now been received from the billing authorities which shows an increase of £2m compared with the previous estimate. These are currently being checked and validated prior to the final position being confirmed.

19. The net changes to the 2022/23 budget total £7.4m, which can be contributed to the budget equalisation reserve to provide cover for budget shortfalls in later years. In addition, the latest assessment of the High Needs Block position for 2023/24 to 2025/26 is reporting a reduction in the deficit due to higher than expected government grant allocations in the Settlement, allowing for reduced contributions to the budget equalisation reserve of £5.7m, £7.1m and £8.3m. The overall High Needs deficit, by the end of the MTFS, is now forecast to be £63m compared with £86m reported in the draft MTFS report to the Cabinet in December 2021.

20. The contribution to the budget equalisation reserve in 2022/23 includes £0.1m to fund a temporary policy officer to implement an anti-racism strategy (£80,000 over 2 years) and to provide funding for Highways closures for the Queens Jubilee celebrations in 2022 (£50,000).

21. The central inflation contingency will be increased by £1.6m in 2022/23 to reflect the Market Sustainability and Fair Cost of Care funding referred to above, and then by a further £2m from 2023/24 for increasing estimates of inflation. Overall this provides £29m for inflation in 2022/23 rising to £72m by 2025/26.

22. Other changes include, the Financing of Capital and the Bank and Other Interest budgets which have been adjusted for the combined effects of -£0.2m in 2024/25 and -£0.8m in 2025/26 due to the latest forecasts on the financing of the capital programme.

23. The above changes have not yet been reflected in the Appendices to this report. The net effect of these changes will be proposed to the Cabinet to be added to the budget equalisation reserve to fund the 2023/24 MTFS deficit. The detailed updates will be included in the updated proposals to the Cabinet on 11th February 2022.

Corporate and Central Items

24. Details of the corporate and central items elements of the MTFS are shown in Appendix B.

DSG (Central Dept Recharges)

25. A total of £2.3m is set aside from the DSG to fund central department costs of Schools.

MTFS Risks Contingency

26. In common with previous years the proposed MTFS includes a contingency of £8m in 2022/23 and later years for other specific key risks that could affect the financial position on an ongoing basis. Examples include:

- The non-achievement of savings.
- Certainty of partner funding, for example services provided through the Better Care Fund (BCF).
- Pressure on demand led-budgets particularly in social care.
- Maintaining the level of investment required to deliver savings.
- New service pressures that arise.

27. When the contingency is released ‘free’ resources are directed toward the Future Developments earmarked fund to reduce the shortfall in capital funding discussed later in this report.

Contingency for Inflation / Living Wage

28. A total of £28.7m has been included in the latest MTFS for 2022/23, rising to £43.4m in 2023/24, £57.8m in 2024/25, and £72.2m in 2025/26. This contingency will be allocated to services as necessary.

29. The main components of the contingency are provisions for:
- Pay awards £22m
- Pension contribution increases £4m
- National Insurance increase £3m
- National Living Wage/ Adult Social Care fee reviews £30m
- Other running costs, net of income £12m (£2m higher than draft MTFS)
- ASC reforms £1.6m (introduced since draft MTFS)

30. The MTFS provides for annual pay awards in 2022/23 onwards of 2.5%, with an allowance for higher increases in the lower Grades to reflect the impact of the National Living Wage (NLW).

31. The central inflation contingency includes provision for an increase of 1% each year in the employers' pension contribution rate, in line with the requirements of the actuarial assessment.

32. The contingency provides for estimated costs of £3m for the impact of the new "levy" for Health and Social Care, which will be an increase to National Insurance in 2022/23, followed by a separate Levy from 2023/24 onwards.

33. The contingency includes provision of £30m for anticipated increases in costs driven by increases in the NLW, with Adult Social Care costs being the main contributor. The Government's stated policy remains for the NLW to increase to £10.50 per hour by 2024, an increase of 18% from the current level (£8.91). There is a risk that the NLW could be higher than £10.50 as it is linked to two thirds of median earnings which could be higher than the Government originally anticipated in 2020.

34. The Government's preferred measure of inflation is the Consumer Price Index (CPI), which the Bank of England is tasked with targeting at a 2% rate. However, the Council's cost base does not always reflect these household inflation measures. Energy and fuel increases, for example, have a much more significant impact. To compensate, the draft MTFS assumes 5% for 2022/23 and 3% per annum inflation over the period 2023/24 to 2025/26 for other running costs. Conversely elements of the County Council's cost base do not inflate. For example debt financing and fixed price contracts, as a result no inflation provision is applied to 25% of the cost base.

35. The level of inflation contingency is assessed on an annual basis. This allows any over or under provision to be adjusted for without balances building, which could be directed to service provision, or unmanageable liabilities growing.

Financing of Capital

36. Capital financing costs are expected to increase to £19.5m in 2022/23 (from £19.0m in 2021/22) and then to rise to £20m in 2023/24, £21m in 2024/25 and £23m in 2025/26. The increase is as a result of increasing financing requirements for the capital programme.

Revenue Funding of Capital

37. The budget includes revenue funding of capital expenditure, mainly for the Corporate Asset Investment Fund and for Future Developments, as described under the capital section later in the report. The latest position includes a total of £2.5m in 2022/23 and £1.5m from 2023/24 onwards.

Central Expenditure

38. The 2022/23 budget includes:

- Pensions (£1.4m) - funding for added years, agreed before and as part of Local Government Reorganisation in 1997;
- Members' Expenses and support (£1.2m);
- Flood Defence Levies (£0.3m) payable to the Environment Agency;
- Elections (£0.2m) annual contribution to an earmarked fund to fund County Council elections;
- Financial Arrangements (-£0.8m) – including income from Eastern Shire Purchasing Organisation (ESPO) surpluses and external audit fee costs. This includes a saving of £150,000 (rising to £250,000 by 2024/25) from growth in ESPO's net income.

Other Income

39. The 2022/23 budget includes a budget of £1.4m for Bank and Other Interest, relating to income from treasury management investments. The forecast increases to £1.6m in 2023/24 and then reduces to £1.3m in 2024/25 and £0.7m in 2025/26, as balances are forecast to be used to fund the capital programme. The levels of interest are based on the expectation that Bank of England base rates will remain at a low level for the foreseeable future.

Corporate Growth and Savings

40. G34 - Corporate Growth contingency - £7.1m in 2023/24, rising to £13.6m in 2024/25 and £20.0m in 2025/26. This has been included to act as a contingency for potential further cost pressures in the later years of the MTFS – the value has been set based upon historic levels of growth incurred. Without the use of such a contingency the County Council is likely to be required to make savings in a very short time period.

Adequacy of Earmarked Funds and Robustness of Estimates

41. The Local Government Act 2003 requires the Director of Corporate Resources to report on:

a) The adequacy of reserves, and
b) The robustness of the estimates included in the budget.

42. The financial environment continues to be challenging with a number of known major risks over the next few years. These include:

- Ongoing impact of Covid 19.
- Higher inflation levels than currently allowed for in the Inflation Contingency.
- Non-achievement of savings and income targets. The requirement for savings and additional income totals £100m over the next four years of which £46m is unidentified. Successful delivery of savings is dependent

upon a range of factors, not all of which are in the control of the County Council.

- The financial positions of Health and Social Care are intrinsically linked and of growing importance. Depending on the financial position of the Clinical Commissioning Groups, the implications for the County Council could be reductions in the funding received through the BCF and additional costs as a result of changes in the NHS, such as the Transforming Care programme that will move more care into the community or the discharge process from hospital.
- Service pressures resulting in an overspend, including demand-led children's and adult social care, particularly on the children's social care and SEN placements budget.
- Continued increase in the National Living Wage, only notified a few months in advance of each financial year. Compounded by higher anticipated wage inflation.
- The strength of the economy dictates the funding of the public sector, both directly through council tax and business rate income and indirectly through the influence on Government funding decisions.
- The increasing reliance on income generated from services in other parts of the public sector. Given the much tighter financial environment for the sector it will be challenging to maintain or keep increasing income.
- 2023 is a year which could see the biggest changes to local government for a generation. The following initiatives are all now planned or anticipated to be implemented in that year, although further delays would not be unexpected:

    - Review of Business Rate retention, including significant new responsibilities and a "reset" of the system's baselines (deferred from April 2020).
    - Fair Funding Review, covering redistribution of funding nationally (deferred from April 2020).
    - Health Integration plans implemented (deferred from 2020).
    - Review of SEND reforms.

43. There are a number of ways that risks will be mitigated and reduced. These are summarised below and explained in more detail in the following paragraphs:

    - General Fund
    - MTFS Contingencies
    - Earmarked funds
    - Effective risk management arrangements.

General Fund

44. The General Fund balance is available for unforeseen risks that require short term funding. The forecast balance on the General Fund (non-earmarked fund) at the end of 2021/22 is £18m which represents 3.9% of the net budget (excluding schools' delegated budgets). It is planned to increase the General Fund to £22m by the end of 2025/26 to reflect increasing uncertainty and risks

over the medium term, and to avoid a reduction in the percentage of the net budget covered. These risks come in a variety of forms:

- Legal challenges such as judicial reviews that require a change in savings approach.
- Legislative changes that come with a financial penalty, for example General Data Protection Regulations (GDPR).
- Service provision issues that require investment, for example the capital investment to support the High Needs Block Development Plan.
- Variability in income, particularly from asset investments.
- Ongoing impact of Covid-19.

Earmarked Funds

45. The estimated balance for revenue earmarked funds (excluding schools and partnerships) as at 31 March 2022 is £85.1m and for capital funding purposes £97.3m, based on the latest information. This is set out in detail in Appendix C to this report. The final level of earmarked funds will be subject to the actual expenditure and any partner contributions, e.g. health funding arrangements and specific grants.

46. Earmarked funds and balances are held for specific purposes in line with the Council's Earmarked Funds Policy attached as Appendix D. The main earmarked funds and balances projected at 31 March 2022 are:

(a) Capital Financing (£97.3m). This fund is used to hold MTFS revenue contributions to match the timing of capital expenditure in the capital programme and also holds the balance of contributions that will be used to fund future developments, mainly capital projects, as they are approved.
(b) Insurance (£13.3m). Funds are held to meet the estimated cost of future claims to enable the County Council to meet excesses not covered by insurance policies. The levels are informed by recommendations by independent advisors. The insurance earmarked funds includes funding for uninsured losses (£5.3m). This is mainly held to meet additional liabilities arising from Municipal Mutual Insurance Ltd (MMI) that is subject to a run-off of claims following liquidation in 1992 and also of other failed insurers such as The Independent Insurance Company.
(c) Budget Equalisation Fund (£40.9m) – fund to manage variations in funding across financial years. This includes the increasing pressures on the High Needs element of the Dedicated Support Grant (DSG) which forecasts a deficit of £28m by the end of 2021/22. The fund includes £7.8m earmarked to offset the forecast 2023/24 net MTFS deficit and a further £5.0m to contribute to the forecast 2024/25 deficit. The intention is to manage these through further ongoing cost reductions.
(d) Transformation (£4.2m). The fund is used to invest in transformation projects to achieve efficiency savings and also to fund severance costs.
(e) Covid-19 Council Tax etc (£4m). The fund will be used to offset any longer term reductions in Council Tax and Business Rates as a result of the economic impacts of the pandemic.

(f) Funds for specific departmental infrastructure, asset renewal and other initiatives (£22.7m).
(g) Pooled Property investments (-£23.6m) – invested against the balance of earmarked funds held.

47. Grant Thornton UK LLP, the County Council's external auditor, has reviewed the level of earmarked funds held by the County Council in respect of financial sustainability as part of its value for money review of the current MTFS and reported no issues In their latest audit Grant Thornton commented that "Leicestershire County Council has a good track record of sound financial management. The Council understands the financial risks which it faces and managed these risks by maintaining an appropriate level of reserves and sound financial management".

School Balances

48. Balances are also held by schools. They are held for two main reasons. Firstly, as a contingency against financial risks and secondly, to save to meet planned commitments in future years. The balance at 31st March 2021 was £9.7m. The balance at 31st March 2022 has not been estimated but is expected to have reduced as a result of spending pressures. It is also affected by the number of schools converting to Academies.

Capital Programme 2022/23 to 2025/26

49. The programme has been updated for the latest programme of deliverability and resources. The overall approach to developing the capital programme is set out in the capital strategy (Appendix E) and is based on the following key principles:

- To invest in priority areas of growth, including roads, infrastructure, climate change, including the forward funding of projects;
- To invest in projects that generate a positive revenue return (spend to save);
- To invest in ways which support delivery of essential services;
- Passport Government capital grants received for key priorities for highways and education to those departments;
- Maximise the achievement of capital receipts;
- Maximise other sources of income such as bids to the LLEP, section106 developer contributions and other external funding agencies;
- No or limited prudential borrowing (only if the returns exceed the borrowing costs).

50. The draft capital programme totals £514m over the four years to 2024/25, shown in detail in Appendix F. The programme is funded by a combination of Government grants, capital receipts, external contributions, revenue balances and earmarked funds.

51. Where capital projects are not yet fully developed or plans agreed these have been included under the heading of 'Future Developments' under each departmental programme. It is intended that as these schemes are developed during the year, they will be assessed against the balance of available resources and included in the capital programme as appropriate. A fund of £60m is included in the draft corporate capital programme.

52. The proposed programme can be summarised as:

Service Improvements	£235m
Investment for Growth	£124m
Invest to Save	£95m
Future Developments	£60m
Total	**£514m**

<u>Funding and Affordability</u>

Forward Funding

53. The County Council recognises the need to forward fund investment in infrastructure projects to enable new schools and roads to be built and unlock growth in Leicestershire before funding, mainly from section 106 developer contributions, is received. This allows a more co-ordinated approach to infrastructure development. A total of £33m in forward funding is included in the proposed capital programme (in addition to £6m in previous years) that is planned to be repaid in the future. When the expected developer contributions are received they will be earmarked to the capital programme, to reduce the dependency on internal cash balances in the future.

54. Forward funding presents a significant financial commitment for the County Council, but should ensure:

- Opportunities to secure external funding are maximised, through successful bids.
- The final cost of infrastructure investment is reduced (compared with what it would be if construction was delivered incrementally as and when smaller developments come forward).
- The design is optimised, to the benefit of the local community.

55. There are risks involved in managing and financing a programme of this size. There is reduced scope for funding additional schemes that are identified in the future. And an increased reliance on developer contributions through section 106 agreements means that it may take many years for investment to be repaid. This could be further compounded in the event of an economic slowdown. To this end, support of district councils is essential to ensure the agreements reached with developers mitigate these risks.

56. Given the benefits to Leicestershire that the increased investment will bring it is considered that district councils should share in these risks in a proportionate way. The County Council continues to work with districts in relation to major

infrastructure schemes being progressed in their areas; district councils will benefit directly through additional tax revenues and increases in Government grants. However, the circumstances around individual projects vary. Hence unique measures need to be put in place to minimise the risks in each district area.

57. The risk with forward funding is that insufficient or delayed contributions, from developers, will fall upon the County Council. A key determinant in generating sufficient developer contributions is the approach taken by the district council, as the planning authority. The district council will set the local planning context against which section 106 agreements will be agreed and ultimately decide on planning permission.

58. A significant problem associated with funding major infrastructure projects is the way in which capital funding is allocated. Significant resource is required to develop bids which may ultimately be unsuccessful. Whilst it is important that robust business cases are developed to ensure the benefits of the project are sufficient to justify the investment, the fact that successful bids usually also need a degree of match/local funding to supplement grant money means that overall tight capital programmes become even more stretched. The County Council considers that such an approach is unsustainable and needs to be reviewed and will continue to raise this with central government.

59. The East Midlands is disadvantaged in terms of the ability to influence Government and attract investment or devolution opportunities compared to the West Midlands. There is an elected mayor and a combined authority for the West Midlands. Their most recent devolution deal (2017) includes £6m for a housing delivery taskforce, £5m for a construction skills training scheme and £250m to be spent on local intra-city transport priorities. The first devolution deal (2015) included over £1bn investment to boost the West Midlands economy.

60. The County Council is pursuing the possibility of a County Deal with Government which would provide a much more stable and sustainable approach to infrastructure decisions to be taken, and allow all funding received to be used in a more cost-effective manner.

Capital Programme Funding

61. The proposed capital programme funding is shown below.

Capital Grants	£191m
Capital Receipts from sales	£24m
Revenue/ Earmarked funds	£93m
External Contributions	£45m
Borrowing (from internal balances)	£161m
Total	**£514m**

Capital Grants

62. Grant funding for the capital programme totals £191m across the 2022-26 programme. The majority of grants are awarded by Government departments including the Department for Education (DfE) and the Department for Transport (DfT).

Children and Family Services

63. Capital grant funding for schools is provided by the DfE. The main grants are:

    a) Basic Need – this grant provides funding for new pupil places by expanding existing schools and academies or by establishing new schools. Funding is determined through an annual submission to the DfE which identifies the need for additional school places in each local authority area. The DfE has announced details of the grant awards for 2022/23 (£8.8m). No details have been announced for future years. An estimate of £3m has been used for 2023/24 to 2025/26.

    b) Strategic Capital Maintenance – this grant provides the maintenance funding for the maintained school asset base. Details of the grant for 2022/23 and future years have not yet been announced. An estimate of £2m per annum is included in the capital programme. It is expected that this grant will continue but will reduce as further schools convert to academy status.

    c) Devolved Formula Capital (DFC) - funding provided to schools. The DfE has not yet announced details of grant allocations. However, an estimate of £0.5m per annum can be made, based on the number of maintained schools.

    d) New (Free) School bid – the programme funding includes an £8m DfE grant to fund a new Social Emotional and Mental Health special school in 2023/24 required as part of the High Needs Development plan.

Adult Social Care

64. Capital funding for the Disabled Facilities Grant (DFG) programme has not yet been announced. An estimate in line with previous years, £4.4m per annum, has been included in the capital programme.

Environment and Transport

65. The DfT grants have not yet been announced and so estimates have been included, based on previous years. These include:

    a) Integrated Transport Block - £2.7m p.a. (£10.9m overall).
    b) Maintenance - £9.9m p.a. (£39.5m overall).

c) Transport Infrastructure Investment Fund (inc. Pot Holes) - £7.9m p.a. (£31.6m overall).

66. Other significant Environment and Transport capital grants included are:

- DfT Melton Mowbray Distributor Road funding - £40.5m (total £49.5m including 2020/21 allocation).
- Housing Infrastructure Fund – Melton Southern Distributor Road - £15.9m (total £18.2m including 2020/21).

Capital Receipts

67. The generation of capital receipts is a key priority for the County Council. The draft capital programme includes an estimate of £24.2m across the four years to 2025/26.

68. The estimate includes potential land sales that are subject to planning permission. In these cases the value of the site is significantly increased when planning permission is approved. However, this also comes with a significant amount of uncertainty and potential for delays. For planning purposes a total of £6m of future estimated sales subject to planning permission has been included.

Revenue / Earmarked Funds/ Contributions

69. To supplement the capital resources available and avoid the need for borrowing £93m of revenue/ reserves funding is being used to fund the programme consisting of:

One-off MTFS 2022-26 revenue contributions	£7m
Departmental earmarked funds	£5m
Capital Financing earmarked fund	£81m
Total	**£93m**

70. The capital financing earmarked fund temporarily holds previous years' revenue contributions to fund the capital programme until they are required.

71. Supplementary funding is required where schemes cannot be fully funded by alternative sources, such as grants. Examples of this are the replacement of operational assets, such as the vehicle replacement programme and ICT systems.

External Contributions and Earmarked Capital Funds

72. A total of £45.6m is included in the funding of the capital programme 2022-26, all relating to section 106 developer contributions.

Funding from Internal Balances

73. A total of £161m in funding required is included within the capital programme to fund the programme and enable investment in schools and highway

infrastructure to be made. Over the next 10 to 15 years it is anticipated that circa £39m of this funding will be repaid through the associated developer contributions.

74. Due to the strength of the County Council's balance sheet, it is possible to use internal balances (cash balances) to fund the capital programme on a temporary basis instead of raising new external loans. Levels of cash balances held by the Council comprise the amounts held for earmarked funds, provisions, the Minimum Revenue Provision (MRP) set aside for the repayment of debt and working capital of the Council. The cost of raising external loans currently exceeds the cost of interest lost on cash balances by circa 1.5%.

75. The overall cost of using internal balances to fund £161m of investment is dependent on what happens to interest rates in the coming years. For example, if the Bank of England base rate rises to 1.5%, it is estimated that internal borrowing will cost around £6.5m per annum by 2025/26, comprising MRP of £4m and reduced interest from investments of £2.5m. If external loans were to be raised instead, the cost is estimated to be £8m per annum on the basis that external borrowing rates would be around 2.5%. But because of the uncertainty on interest rates, this position will be kept under review as part of the treasury management strategy.

76. The County Council's current level of external debt is £263m. As described above this is not assumed to increase during the MTFS. The relative interest rates and cash balances will be kept under review to ensure that this is the right approach.

Capital Programme - Summary by Department

77. Over the period of the MTFS, a capital programme of £514m is required of which £141m is planned for 2022/23. The main elements are:

- Children and Family Services - £94m. The priorities for the programme are informed by the Council's School Place Planning Strategy and investment in SEND as part of the High Needs Development Plan.
- Adults and Communities - £27m. The programme includes £18m relating to the Disabled Facilities Grant (DFG) programme and schemes for the Social Care Investment Plan (SCIP).
- Environment and Transport - £226m. This relates to major schemes such as Melton Mowbray Distributor Road North/East and Southern Sections, Zouch Bridge replacement as well as the Transport Asset Management Programme and the Environment & Waste Programme. Other significant projects include Melton Depot replacement, vehicle replacement and advanced design.
- Chief Executive's - £0.7m, mainly Leicestershire Community Grants.
- Corporate Resources - £12m. This mainly relates to investment in ICT, transformation, property and environmental improvements.
- Corporate Programme - £154m. Investment includes the Corporate Asset Investment Fund (CAIF), the Future Developments fund (subject to business cases), and Major Schemes Portfolio Risk.

Changes to the Capital Programme 2022-26

78. Since the report to the Cabinet, the overall borrowing requirement is proposed to reduce from £161m to £143m following a review of reserves and contingencies held for Covid19 which are no longer expected to be required. The latest position shows that it is looking as though much of this provision will not be required and can be freed up to fund additional one-off expenditure. This includes; the £8m remaining balance from the Covid-19 and MTFS risks 2021/22 provision, reported to the Cabinet on 14th December 2021, and £5m set aside in the Council Tax / Business Rates losses reserve at year end in 2020/21.

79. The expenditure profiles on all schemes are also being reviewed and updated to reflect the last known position.

80. The above changes have not yet been reflected in the Appendices to this report. The detailed updates will be included in the updated proposals to the Cabinet on 11th February 2022.

Corporate Asset Investment Fund (CAIF)

81. As reported in the CAIF Annual Update to the Cabinet in September 2021, the Fund's value has grown year on year and as the value of the Fund increases, so the income produced also continues to grow and last year the Fund generated a net income of £4.6m. As at 31st March 2021, the capital value of the portfolio totalled £187.4m compared with the value as at 31st March 2020 of £170.9m (a 9.6% increase) during the period most impacted by the COVID-19 virus.

82. The strategy for the CAIF is reviewed regularly but the key objectives of the strategy remain:

    - Ensuring that there is a diverse range of assets available to meet the aims of economic development.
    - Increasing the size of the portfolio.
    - Improving the quality of the assets.
    - Ensuring the sustainability of the County Farms and industrial portfolios by replacing land and assets sold to generate capital receipts.
    - Providing a revenue stream that can be used to support ongoing service delivery; and
    - Ensuring that any development undertaken on land owned by the County Council (or sold to a 3rd party for development) is undertaken in accordance with the aims and aspirations of the County Council's
    - Declaration of Climate Emergency and any development is therefore to be sustainable, low carbon and energy efficient.

83. An independent review of the Fund undertaken by Hymans Robertson in December 2020, and reflected in the current strategy, considered the current economic outlook and that of the real estate investment market in light of the COVID-19 crisis and the implications of Brexit. In line with other commentators, it acknowledged the challenges facing the market at the present time particularly the retail sector. Equally, it identifies the industrial, distribution and logistics

sectors as being the most resilient in current circumstances. Further, the report examined the potential to diversify the portfolio further by considering infrastructure investments and the need to consider the environmental, social, and governance credentials of future potential investments.

84. Broadly, the Hymans Robertson report made the following main recommendations:

- Investment in direct property assets should be focused on the industrial, distribution and logistics sectors especially given Leicestershire's location at the heart of the national transport network.
- Investment in the office and rural sectors should be maintained at current levels.
- Investment in the Pooled Property sector should be reduced over time and the funds reinvested in other more attractive investments such as diversified infrastructure. The private debt investments have potential to deliver stable returns and should be maintained or increased.
- Consideration should be given to investing in infrastructure and renewables either directly or via a pooled investment vehicle. Entry into the residential market is also recommended. To an extent the portfolio has an exposure to the residential market through the bringing forward of development sites However, the development and retention of residential properties within the portfolio would present particular legal problems for the County Council not being a housing authority.

85. These recommendations continue to be implemented and didn't require and significant change in strategy. The strategy will be updated next year, taking into account the latest market trends and the County Council's strategy development. The review should be in a position to address both the short-term effects and potential longer-term impact of the COVID-19 pandemic with a view to protecting the Fund's current portfolio and guide its future acquisitions strategy and development programme moving forward to ensure it maximises the benefits it delivers. A copy of the updated strategy for 2022-26 is attached as Appendix G.

<u>Freeport</u>

86. The County Council is acting as Lead Authority in relation to the establishment and ongoing activity of the East Midlands Freeport (EMF). The final business case is required to be submitted to the Department for Levelling Up, Housing and Communities (DLUHC) by the end of February 2022 with a likely designation of EMF from April 2022.

87. During the current year the County Council has funded costs around business case development and wider set up costs. Net costs are expected to total around £1m by the end of this current financial year. Agreement has been reached that any costs incurred by the County Council will be recovered from future retained business rates once the sites are up and running. However, this does mean that the County Council is required to cash flow at risk of non-designation.

88. The governance arrangements going forwards are currently being developed through an EMF constitution, which will be agreed and signed off by the EMF Board in the near future. The constitution will include measures to protect the overall financial exposure of the County Council in its capacity as Lead Authority/Designated Body. As part of this, consideration is being given to how EMF governance will link in with that of the East Midlands Development Corporation (The Integrated Rail Plan published in November referred to ‘accelerating a delivery vehicle’ for the sites identified by the Development Corporation.).

89. The County Council has committed £500,000 per annum, for three years, to the Development Corporation. This contribution will need to be kept under review, depending upon progress of the venture and commitment of local and national partners.

Budget Consultation

90. The Cabinet at its meeting in December 2021 approved the MTFS proposals for consultation. The consultation asked for views on the savings plan and the appetite for Council Tax increases. The consultation closed on 16th January 2022. There were 139 response which are currently being analysed. A report on the outcome will be included within the MTFS report to the Cabinet on 11 February 2022.

Results of Scrutiny Process

91. The Overview and Scrutiny Committees and the Scrutiny Commission have received detailed reports on the revenue budget and capital programme proposals, which can be viewed via the County Council’s website (www.leicestershire.gov.uk). A summary of the comments arising from the meetings of Scrutiny bodies will be presented with the MTFS report to the Cabinet on 11 February 2022.

Equality and Human Rights Implications

92. Public authorities are required by law 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; and
- Foster good relations between people who share protected characteristics and those who do not.

93. Many aspects of the County Council's MTFS may affect service users who have a protected characteristic under equalities legislation. An assessment of the impact of the proposals on the protected groups must be undertaken at a formative stage prior to any final decisions being made. Such assessments will be undertaken in light of the potential impact of proposals and the timing of any proposed changes. Those assessments will be revised as the proposals are developed to ensure that decision-makers have information to understand the

effect of any service change, policy or practice on people who have a protected characteristic.

94. Proposals in relation to savings arising out of a reduction in posts will be subject to the County Council's Organisational Change policy which requires an Equality Impact Assessment to be undertaken as part of the Action Plan.

Crime and Disorder Implications

95. Some aspects of the County Council's MTFS are directed towards providing services which will support the reduction of crime and disorder.

Environmental Implications

96. The MTFS will include schemes to support the Council's response to climate change and to make environmental improvements.

Partnership Working and Associated Issues

97. As part of the efficiency programme and improvements to services, working with partners and service users will be considered along with any impact issues, and they will be consulted on any proposals which affect them.

Risk Assessments

98. As this report states, risks and uncertainties surrounding the financial outlook are significant. The risks are included in the Corporate Risk Register which is regularly updated and reported to the Corporate Governance Committee.

Background Papers

Report to the County Council on 17th February 2021: Medium Term Financial Strategy 2021/22-2024/25 - https://politics.leics.gov.uk/documents/s159779/Revised%20Cabinet%20Report%20MTFS%202021-25.pdf

County Council Strategic Plan – https://www.leicestershire.gov.uk/about-the-council/council-plans/the-strategic-plan

Report to the Cabinet on 14th December 2021: Medium Term Financial Strategy 2022/23 – 2025/26 – Proposals for Consultation – https://politics.leics.gov.uk/ieListDocuments.aspx?CId=135&MId=6449&Ver=4

Appendices

Appendix A: Four Year Revenue Budget 2022/23 to 2025/26
Appendix B: Corporate and Central Items Revenue Budget 2022/23
Appendix C: Earmarked Funds Balances
Appendix D: Earmarked Funds Policy

Appendix E: Capital Strategy
Appendix F: Draft Capital Programme 2022/23 to 2025/26
Appendix G: Corporate Asset Investment Fund Strategy 2022/23 to 2025/26

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