

CABINET

27th September 2004
B

ASE BUDGET PREPARATION 2005/06

REPORT OF THE CHIEF FINANCE OFFICER

1. **Purpose of Report**

This report explains the process by which the Council's 2005/06 base budget is being prepared, and summarises the principles supporting this process.

2. **Summary**

- 2.1 The first step in agreeing the 2005/06 revenue budget is to prepare a rolled forward base budget. This is entirely a mechanical exercise: it expresses the financial impact of decisions previously taken by the Council, at 2005/06 prices and does not anticipate any later decisions the Council may take about the budget. As in previous years, the Chief Finance Officer has established the framework for base budget preparation, and these principles are summarised in the attached supporting information.
- 2.2 As for 2004/05 the Authority is adopting a "cash-limited" approach to budgeting. Each department is set a cash limit for its base budget, reflecting assumptions made on inflation and other factors requiring to be taken into account. **Each department's base budget must be prepared within this cash limit.** Any budget pressures identified by departments which cannot be contained within the cash limit will lead to proposals for service developments, which will need to be dealt with in the context of those department's budget strategies.
- 2.3 There are areas of uncertainty at this stage that are likely to result in further changes to departmental cash targets. These include services presently supported by specific government grant, which are likely to transfer into mainstream funding, and the effect of the forthcoming revaluation of the Leicestershire pension fund (the results of which will be known in the Autumn). Examples of the former are Preserved Rights grant and the residential allowance, which could both affect the Social Care and Health Department. These adjustments will be made when their full implications are known.
- 2.4 Having agreed cash limits the base budget should be completed by December. Cash limits for each department are shown at Appendix A, and the changes between 2004/05 and 2005/06 are summarised below:-

Changes in Cash limits from 2004/05 to 2005/06

ITEM	£'000
Net budget 2004/05 (Service Departments)	338,043.7
Full Year Effects	(1,742.6)
Inflation	9,603.3
Pensions	230.0
Other changes	45.0

Budget 2005/06 (Service Departments)	346,179.4

2.5 Members are asked to note that the cash limits issued to each department do not constitute the whole of the Council's revenue budget, as there are certain corporate items which are managed centrally. The 2004/05 budget shown in appendix A can be balanced back to the table on page 11 of the Council's budget book as follows:

	£'000
Service department budgets	338,043.7
Corporate budgets	6,941.6
Net recharges	(2,600.1)
Capital charges	13,866.7

	356,251.9

3. Recommendations

3.1 Cabinet is asked to:

- i) endorse the framework for base budget preparation;
- ii) approve the cash limits for each department.

4. Financial and Legal Implications

4.1 The report outlines the framework for base budget preparation and the resulting base budget for departmental service spending.

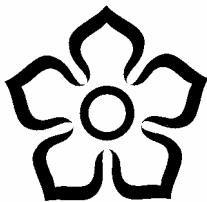
4.2 There are no direct legal implications in this report. Peter Nicholls, the Head of Legal Services has been consulted in the preparation of this report.

5 Report Author/Officer to contact:

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DECISION STATUS

Key Decision	No
Reason	N/A
Appeared in Forward Plan	No
Executive or Council Decision	Executive (Cabinet)



Leicester
City Council

**WARDS AFFECTED:
ALL WARDS (CORPORATE ISSUE)**

CABINET

27 September 2004

BASE BUDGET PREPARATION 2005/06

SUPPORTING INFORMATION

1. Purpose of the Report

- 1.1 The report provides background information on the framework for preparation of the 2005/06 base budget.

2. Details of Framework for Base Budget Preparation

- 2.1 The key points of the framework are:

- The base budget is prepared on a “volume standstill”: no adjustment will be made for demographic or other changes to client groups which must be dealt with through departments’ budget strategies;
- The full year effects of previously approved budget reductions and growth will be incorporated in the base budget (i.e. where an approved change to the budget was time-limited, or has greater effect in 2005/06 than in 2004/05);
- An allowance for inflation has been added to the base budget based on the following assumptions:

⇒ teachers’ salaries, NI and pension costs:	2.95%
⇒ other salaries, NI and pension costs:	2.95%
⇒ other running costs (including levies from external organisations):	2%
⇒ income (exc. Government Grants):	2%

Unusually, the inflation factors used for pay reflect agreed pay awards rather than estimates (as multi-year pay deals have been negotiated).

The inflation assumptions used for running costs needs some discussion this year, given the introduction of the new “Consumer Prices Index” (CPI) as the Government’s standard measure of inflation late in 2003/04. Prior to this year there were two main indicators of price inflation:-

- a) the Retail Prices Index (RPI), which we have never used because it includes mortgage interest payments;

- b) RPIX, being the equivalent of the RPI without mortgage interest. This was previously the standard measure which the Bank of England was expected to target at 2.5%.

At present RPI stands at 3% and RPIX at 2.2%.

The new measure (CPI) is constructed differently to, and will always be lower than RPIX, and hence the Bank of England is expected to target 2.0% (the CPI presently stands at 1.4%). It needs to be considered whether or not the new measure should be applied in the budget. In doing so, of course, it must be remembered that the actual cost of providing services does not change simply because the Government changes the way inflation is measured.

In practice both RPIX and the CPI have some deficiencies in a local authority context:-

- a) RPIX includes depreciation of housing, and council tax which are not applicable to local authorities;
- b) the CPI is constructed on the basis of a different averaging method, reflecting the way consumers respond to price changes (eg by buying less) which are not applicable to the Council. It also reflects the price reductions arising from international competition for items such as clothing and CDs which benefit the consumer far more than local authorities.

There is a fourth measure (the GDP deflator) which is a much broader measure than either the CPI or the RPIX. It is less well understood and more volatile.

The estimate of 2% used in cash targets for running costs / income is closer to present (and forecast) RPIX, but is also the target measure for the CPI. It is not felt appropriate to recommend a measure closer to CPI, particularly given expected increases in energy costs.

The inflation provision also recognises the employee element of internally traded services contained within departmental running costs budgets;

- No allowance is made for Officers' pay increments. Departments are expected to fund these through savings made by natural turnover of staff;
- A review of the County Council superannuation fund by the actuaries is currently being undertaken and there is expected to be an increase in employer's contributions. The base budget will be adjusted when the position is more clear. For the time being, an estimate has been used;
- Allowance is made for sundry other items, shown in the "other changes" line in the Table. These include:-
 - an allowance of £0.1m for reductions in rental income arising from disposals of property required to finance the Capital Programme;
 - an allowance of £0.2m for an increase in the level of landfill tax;
 - an allowance of £0.1m for a change from grant funding to mainstream funding for the civil defence grant;
 - an adjustment of (£0.4m) to realign the non-operational property budget

- Virement has taken place between departments since the 2004/05 budget was set and reflects the transfer of responsibility or funding for services between departments. Further virements will occur as details of service transfers are finalised. There is no overall effect on the General Fund budget as a consequence of such transfers.

3. Other Implications

OTHER IMPLICATIONS	YES/NO	Paragraph within Report	References
Equal Opportunities	No		
Policy	No		
Sustainable and Environmental	No		
Crime and Disorder	No		
Elderly and People on Low Incomes	No		
Human Rights Act	No		

4. Background Papers

General Fund Budget and Council Tax 2004/05; report to the Council 25/2/04 and accompanying budget book.

5. Details of Consultation

Heads of Finance in all Departments have been consulted about the calculation of the cash targets.

6. Report Author/Officer to contact:

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CASH LIMITS FOR BASE BUDGET PREPARATION 2005/06

DEPARTMENT	Original Base 2004/05	Full Year Effects	Inflation Provision	Pensions	Other Changes	Virements	Original Base 2005/06
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Chief Executive's	2,546.5	(150.0)	61.5				2,458.0
Education – Schools Block	152,646.0	196.0	4,312.9	230.0			157,384.9
Education – LEA Block	28,941.8	(1,063.6)	795.0				28,673.2
Housing	6,636.1	(519.6)	294.7			(20.0)	6,391.2
Regeneration & Culture	49,772.0	(2,204.4)	1,278.0		206.0		49,051.6
Resources, Access & Diversity	15,851.7	(50.0)	465.5		(161.0)	20.0	16,126.2
Social Care & Health	81,649.6	2,049.0	2,395.7				86,094.3
	338,043.7	(1,742.6)	9,603.3	230.0	45.0	0.0	346,179.4