HAMPSHIRE COUNTY COUNCIL

Decision Report

Decision Maker:	Cabinet County Council
Date:	15 November 2024 28 November 2024
Title:	Medium Term Financial Update
Report From:	Chief Finance Officer and Director of Corporate Operations

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Section A: Purpose of this Report

1. The purpose of this report is to update Cabinet and County Council on the financial forecasts for the next two financial years, taking into account the latest information from the in-year monitoring and importantly the impact of the 30 October budget announcement and what that means for 2025/26 budget setting.

Section B: Recommendation(s)

It is recommended that Cabinet:

2. Notes the limited impact of the Autumn Budget on the County Council's financial position.

3. Notes the increase in the gross gap for 2025/26 which is now forecast to be £182m after assuming an increase of £8.7m in social care grant, the reasons for which are set out in the report.

4. Unless the Government's proposed November Policy Paper on Local Government Finance provides a change in legislative requirements, freedom and flexibility as requested by the Leader in his letter to the Chancellor (see appendix 1) and provides council tax flexibility to allow for an above 5% council tax increase, then Cabinet agrees that the Leader will write to the Government to further emphasise the Council's financial position, request formal talks and ask for Exceptional Financial Support for 2025/26, in the form of an allowable increase in council tax above the referendum limit.

5. Approves participation in a Business Rates Pool in 2025/26 with 5 District Councils within Hampshire expected to yield around £4.3m additional business rates for the County Council next year.

6. Approves £2m of funding for the development and implementation of a digital programme through a dedicated project team to drive process efficiency and to deliver digitally enabled savings. Funding to be top sliced from the review of IT reserves outlined in this report.

7. Delegate authority to the Director of Corporate Operations in consultation with the Chief Executive to approve spend for the digital programme on a business case basis, provided that each business case delivers either a direct saving or indirect savings (for example removing failure demand).

8. Notes the urgent financial decisions taken in respect of the Manydown Development under Financial Regulations by the Chief Financial Officer as outlined in paragraph 199.

9. Approves a total of £1.816m for further Manydown spend as outlined in paragraph 202 and grants approval to spend of these amounts during the year. This expenditure to be met from the freed up capital resources outlined elsewhere in this report.

10. **Cabinet Recommends that County Council:**

    a) Gives approval to spend up to the value contained in the capital programme for Manydown C and D loan notes that will be drawn down (repaid, transferred or converted) in line with the financial deal with Urban & Civic and Manydown 2018 Ltd.

    b) Approves the proposed changes to the funding and associated schemes within the Capital programme as set out in section M, to release revenue funding of £38.257m, to support an allocation of £28.257m to the Budget Bridging Reserve and retention of £10m as a capital contingency.

    c) Approves the changes in reserves and the transfers to the Budget Bridging Reserve as outlined in Section M.

RECOMMENDATIONS TO COUNCIL

Council is recommended to:

a) Approve spend up to the value contained in the capital programme for Manydown C and D loan notes that will be drawn down (repaid, transferred or converted) in line with the financial deal with Urban & Civic and Manydown 2018 Ltd.

b) Approve the proposed changes to the funding and associated schemes within the Capital programme as set out in section M, to release revenue funding of £38.257m, to support an allocation of £28.257m to the Budget Bridging Reserve and retention of £10m as a capital contingency.

c) Approve the changes in reserves and the transfers to the Budget Bridging Reserve as outlined in Section M.

Section C: Executive Summary

11. The forecast MTFS position set out in this report is caveated on the basis that the Chancellor's Autumn Budget did not fundamentally address any of the issues raised both specifically by the Leader (see the Leader's pre budget letter to the Chancellor – Appendix 1 - which set out a whole range of measures which if implemented would significantly enable Hampshire to manage down demand and reduce spend) nor by Local Government generally, so did not provide:

- any of the new freedoms or flexibilities requested which would have enabled Hampshire to take action to mitigate the financial challenges we face (for example, freedoms on charging for services and means testing).
- any change to outdated or unhelpful legislation which drives demand without accompanying funding (for example Special Educational Needs (SEN) legislation introduced in 2014 that is driving SEN administration costs and importantly the significant rise in school transport).
- any new proposals to allow Councils to raise council tax above the current referendum limit of 5%.

12. Unless the Government's proposed November Policy Paper on Local Government Finance positively addresses the above issues, then the forecast budget position is as set out in this report, and the proposals for discussion with Government on Exceptional Finance Support will need to be taken forward.

13. **The net forecast gap for 2025/26 is £116.2m,** which is net of the impact of the £84.2m SP25 savings already agreed (of which £66.0m is delivered in 2025/26) and assumes £8.7m of additional social care grant.

14. Given the size of the net budget gap at £116.2m, **it is pretty clear that as signposted and anticipated for some time, the County Council has reached the point where it is unable to find the level of savings required to balance the budget on a recurring and sustainable basis.**

15. The position not surprisingly worsens for 2026/27, where the net gap after agreed SP25 phase 1 savings is £185.3m.

16. Given the position, an in depth review of reserves and the revenue funding of the capital programme has been undertaken, and this has enabled nearly £65m of revenue reserve transfers to bolster the Budget Bridging Reserve (BBR); post this review the balance on the BBR is now just under £92m.

17. Whilst the council will review all options for balancing the 2025/26 budget (as set out later on this report, section L), if the BBR was utilised in full as part of reducing the budget gap, this would reduce the budget gap to £24.3m, as shown below:

	2025/26 £m	2026/27 £M
Gross Budget Deficit	182.2	266.4
Less SP25 Phase 1 Savings	(66.0)	(81.1)
Net Recurring Budget Gap	**116.2**	**185.3**
Apply BBR	**(91.925)**	
Revised Budget Gap	**24.275**	**185.3**

18. Even after utilising the full balance on the BBR, there is still a budget shortfall of just over £24m for 2025/26, so as a minimum if the only option available to balance the budget was additional savings, then as a minimum new savings will need to be brought forward for implementation for 2025/26 of £24.3m.

19. As members will be aware, the Chief Officers Management Team have been reviewing the Council's Core Purpose (see section E), and reviewing all services as part of the Legal Minimum Service Level review exercise, and whilst this work is still in progress, there is a level of confidence that the outcome will be an identification of additional savings (referred to SP25 Phase 2 savings) of at least £24.3m, which would allow the budget to be balanced for 2025/26.

20. However, whilst there is a confidence that the 2025/26 budget can balanced, it remains the case that unless the government allows:

- Hampshire freedom and flexibilities over charging and/or
- Implements the changes to legislative requirements set in the Leader's pre autumn budget letter to the Chancellor (see appendix 1)

  together with:

- A significant increase to the funding the council receives (particularly on the back of the spending review next year which the government have set out will include broader redistribution of funding through a multi-year settlement from 2026/27) and/or
- change (increase) to the allowable council tax increase for either 2025/26 or 2026/27,

21. **Then it is pretty clear that the council would need to issue a Section 114 notice for 2026/27**.

22. The financial pressures faced by the County Council are well documented and earlier this year the two year gap to 2025/26 was increased from £132m (November 2023) to at least £175m (July 2024) following the 2023/24 outturn

position that showed increased growth and price increases across social care services and school transport.

23. Detailed monitoring during the current year and early budget preparation work have shown that as at the end of Month 5 (August), **the forecast net overspend after utilising all corporate contingency (£24.5m) for 2024/25 is £15m** (which includes a combined forecast overspend of £47m for Adults Health and Care and Children's Services); the Council has implemented stringent in-year 'spend controls', with the aim of managing down the forecast position towards breakeven, and further detail is set out in section F.

24. There will be a resultant impact on 2025/26 as this in-year forecast pressure flows through in full to next year, and this is the main reason that the gross forecast budget gap before SP25 savings has increased further to £182.2m. Further detail is set out in sections G and I.

25. As a sector Local government has been waiting for announcements on funding from the new Government and in particular, the budget statement on 30 October.

26. From a County Council perspective, the budget announcement was very disappointing. It provided only £1.3bn of additional funding for local government for 2025/26, comprised of £600m for social care and £700m of unspecified funding, alongside an announcement that some of this additional funding would be allocated in a targeted manor based on deprivation. This new funding of £1.3bn is in stark contrast to the additional investment announced for the NHS, which was £22bn.

27. Prior to the budget announcement the Secretary of State for Local Government and English Devolution had set out on the 28 October in a Commons debate that the government '*would focus on aligning funding with deprivation levels, through an "**initial rescue operation"** in this year's financial settlement*'.

28. It is clearly concerning regarding the quantum of new funding of £1.3bn being regarded as a rescue package, relative to the size of the estimated budget shortfall across local government, and the number of council's who have indicated they are in financial difficulty, who without substantial additional funding were forecasting either having to request Exceptional Finance Support or worse case issue a Section 114 (S114) notice. To put this in context Hampshire's revised gross gap of £182m represents nearly 14% of the total additional resources provided for core services nationally.

29. The budget also set out that local government would receive a 3.2% increase in core spending power, inclusive of this additional £1.3bn funding, an assumed average council tax increase on 4.8%, and an average increase in council tax base of 0.8%.

30. For the County Council, the budget offered little in terms of additional funding (best estimate is additional funding of £8.7m), and is far from a 'rescue package', leaving the council with a significant forecast budget shortfall for 2025/26 as set out above.

31. It is disappointing to note that despite the extensive lobbying which the local government sector has undertaken with the government, and the specific lobbying which the County Council has made through the Leader, who wrote directly to the Chancellor in October, many of the concerns raised by the sector, which covered not just the need for increased funding but also reforms which could help manage down demand, have either been ignored or pushed out to be dealt with in reviews to be covered under 'phase 2 of the spending review in Spring 2025', which will be too late to impact the 2025/26 budget.

32. A copy of the Leader's letter to the Chancellor's is attached as Appendix 1 to this report**.** Further detail on the budget announcement and its impact are set out in section H.

33. Given the remaining budget shortfall of £116.2m, in the short term, the council will need to look at all available options for balancing the 2025/26 budget, to ensure that a S114 notice is avoided for 2025/26, as this will at least allow the council to consider the outcome from the review of the local government funding formula and the introduction of 3 year settlements.

34. Over the course of the last 9 months, in light of our worsening MTFS forecast, significant work has been undertaken by the Chief Officers Management Team, undertaking a range of work aimed at supporting the 2025/26 budget position, as set out below:

- Officers have been working on a further set of savings, based on the County Council returning to its 'core purpose' and considering what further SP25 Phase 2 savings could be made if we delivered services at the legal minimum. Officers are also working on bringing forward income generation proposals, which are commercially 'good business'.

  These proposals will cover Directorate as well as one organisation/cross cutting opportunities. The results of this exercise will be reported through the decision making process throughout January and February and will ultimately feed through to the setting of the budget and council tax at County Council on 13 February, but as set out above in paragraph 19 it is anticipated that a minimum of £24.3m of additional savings can be proposed for 2025/26.

- Officers have been reviewing reserves and the capital programme (see section M) to free up additional resources to help balance the budget on a temporary basis and further details are outlined in this report. As set out above, **it is anticipated that there should be sufficient reserves available within the BBR to significantly close the budget gap for 2025/26, albeit on a one-off basis.** Clearly, this will significantly limit the Council's opportunity to utilise reserves in future and is not in any way a sensible or sustainable way to manage the finances of an organisation which spends over £2.5bn every year.

- The Chief Financial Officer (CFO) has also reviewed the opportunity of the County Council entering into a Hampshire Business Rates Pool (BRP), and has concluded that creating a BRP for the 2025/26 financial year, which encompasses the County Council plus 5 district councils, provides a significant one off benefit of potentially around £4.3m; the CFO is recommending as part of this report that the County Council commits to being within the proposed Hampshire BRP for 2025/26, and further detail is set out in section I.

35. Whilst there is the option of substantially closing the budget gap through an unplanned draw from reserves through use of the BBR, this would pretty much mean utilising all spare resources available, and seriously depleting financial resilience. It would leave the Council with very little wriggle room, and all other things being equal and no change in our funding position, would make the prospect of issuing a Section 114 notice almost an inevitability for 2026/27.

36. If the budget was partly balanced through fully drawing down the sum of £91.925m from the BBR, this would take the cumulative draw since 2022/23 to £254.83m; the draw has increased each year, significantly depleting reserves, and is not sustainable:

	Draw from BBR to Balance the Budget **£M**
2022/23	38.00
2023/24	50.80
2024/25	74.10
2025/26	**91.93**
Total Draw	**254.83**

37. It is therefore imperative that Cabinet and Full Council consider the full range of options available to balance the 2025/26 budget in order to minimise the use of reserves, and the options which potentially could be considered include:

- **Further lobbying** - to seek change either as part of the November Policy Statement or within the Provisional Local Government Finance settlement in December. This will include legislative change to decrease demand, freedoms and flexibilities on charging and levels of council tax increase.
- **Exceptional Finance Support** – If the above changes are not forthcoming, to open discussions with the Government on seeking Exceptional Finance Support (EFS) for 2025/26, such support to be by allowing the Council to raise council tax above the 5% referendum limit but without recourse to a referendum (this approach has been allowed in other financially stressed authorities).
- **Council Tax Referendum** - if the option of EFS is not agreed by government, there remains an option to propose a council tax rise

above 5%, and to seek a referendum to be conducted in May 2025 or May 2026.

38. The options are not mutually exclusive, as a mix of a one-off draw from reserves could be utilised (albeit the preference would be to limit the use of reserves) alongside either EFS or a council tax referendum. Further detail on the above options for closing the budget shortfall are set out in section L.

39. The report also reminds Members of the position on Dedicated Schools Grant which indicates that by the end of 2025/26 (when the statutory override comes to an end) there will be a cumulative deficit of £287m and a recurring annual deficit of around £100m. Without significant Government intervention, the County Council would in any event need to issue a Section 114 notice for 2026/27 if there is no solution forthcoming for DSG. Further information is set out in sections G and H.

Structure of the MTFS

40. The MTFS update contains a number of complex and linked issues and a table of contents has been provided below to aid navigation through the report:

Section D: Background and Context

41. The background and context to this medium term financial update is well documented. The national system of funding local government is recognised as not being fit for purpose with a 'fair funding review' being promised since 2016 but never delivered.

42. As an Authority Hampshire no longer receives any general grant from the Government and our annual inflation and growth costs far outstrip what we are able to raise in council tax and retained business rates.

43. Social care spend has always been a pressure area for the County Council, but more recently the impact of Special Educational Needs (SEN) on both the Dedicated Schools Grant (DSG) and school transport is fast becoming the biggest pressure area that the council faces.

44. In round terms annual cost pressures outstrip council tax by at least £60m to £70m a year meaning that the only sustainable way of balancing the budget has been by making savings or raising income locally.

45. After 14 years of making savings totalling some £724.2m to 2025/26 (including the SP25 agreed savings of £84.2m as set out in section J) **not surprisingly, the County Council believes that it has reached the point where it will not be able to make sufficient savings to meet the recurring gaps that occur each year**.

46. Prior to this update to the MTFS, the budget gap for 2025/26 had been estimated to be a shortfall of £132m (November 2023), which net of the full year SP25 savings now agreed of £84.2m would have meant a revised budget shortfall of around £47.8m.

47. As set out in this update, following the outturn position in 2023/24, and the in-year forecast outturn position based on Month 5 budget monitoring, it is clear that the service pressures we face are increasing at a greater rate than expected, resulting in a gross forecast gap after assumed extra social care grant of £8.7m of £182.2m, which after accounting for the agreed SP25 savings of £84.2m (of which £66m is delivered for 2025/26), leaves a budget gap of £116.2m.

48. It has therefore been necessary to look at further options to help close the budget gap, and Officers have been considering what further savings could be made if we were to return to our core purpose and provide services to the legal minimum level (and these savings are referred to as SP25 Phase 2 savings) alongside reviewing what other options could be utilised, and these are set out in section L 'Options for Closing the Budget Gap'.

49. The Government delivered its budget announcement on 30 October following much speculation on possible options they were considering in the run up to the announcement. Key items for local government and how they relate to HCC are set out in section H, but in short there was very little in the way of additional funding for 2025/26 and the rest of this report examines the overall updated position as we head towards 2025/26 and considers our prospects for 2026/27.

Section E: Returning to our Core Purpose

50. Previous reports to Cabinet and County Council have outlined the need to consider what further savings could be made if we were to deliver services at the Legal Minimum Service Level (LMSL). Officers have been working on this premise over the Summer and have produced a significant body of evidence covering 177 separate service lines to evidence the thought processes and outcomes of this exercise, challenged and supported by an Independent Panel, many of whom are already commissioners in other authorities and are very experienced in this sort of role.

51. The scale of this exercise should not be underestimated and it is probably the most comprehensive piece of work that has been undertaken for this type of exercise anywhere in Local Government.

52. The key problem is that whilst regulations place many statutory requirements on local government, they are rarely defined in any detail (if at all) leaving local authorities to interpret what must be provided to meet that statutory duty.

53. Officers have been working across 4 separate service categories (as set out below), and a description of each of the categories is set out in Appendix 2. The number against each category below is the total number from the 177 service lines which meet the definition.

    - Statutory (100)
    - Discretionary Preventative (10)
    - Enabling (47)
    - Discretionary (20)

54. The results of this exercise will be reported to Executive Members, Cabinet and County Council in January and February next year as part of the budget setting process, but the exercise itself has prompted consideration of what the County Council's core purpose is going forward and the reflection that even under legal minimum service levels, the County Councill will still be a £2.5bn a year business providing services to the most vulnerable in our society and providing a range of other statutory services and discretionary ones where they are able to cover their own costs from income.

55. **What is becoming clear though is that even if the Council were operating with all services at the their legal minimum service level in line with the definitions set out in Appendix 2, the council would not be able to balance the budget on a sustainable and recurring basis, a position which is supported by the work of the Independent Panel.**

56. A policy position based around returning to our core purpose is contained at Appendix 3.

Section F: Current Year Position - General Fund

57. As set out in the Quarter 2 (based on month 5 to August) Forecast outturn report (presented elsewhere on the Cabinet agenda), the forecast outturn position is an overspend of £15m, after utilising corporate contingency of £24.5m.

58. It is important to note that despite a significant increase in the Adults' and Children's base budget for 2024/25, they still have a combined forecast overspend of £47m which is contributing to the net overspend of £15m, the consequences of which do impact and feed through to the budget projection for 2025/26.

59. **Spend Controls:** Strict in year spending controls have been put in place from September 2024 with the aim of reducing the overspend, although it is noted that the majority of the forecast overspend is due to increased demand within Adults' Health and Care, Children's social care and Home to School transport; this demand will feed through to the 2025/26 budget and is reflected in this MTFS update.

60. The key message to staff and budget managers on spending controls is that money should only be spent on business critical and unavoidable activities. Specific actions include:

- Recruitment controls including a freeze on non-business critical posts and Director level sign off for all recruitment.

- Non pay spend controls, including ceasing all non-business critical spend.

61. Whilst the focus remains on minimising the in-year overspend, if required the net overspend could be met from the Budget Bridging Reserve (BBR). Any reduction that can be made in the draw for the current financial year provides funding to support the budget in future years.

Section G: Current Year Position - DSG

62. The forecast overspend of £15m set out above does not include the DSG deficit; there is a statutory override in place until the end March 2026 which allows the DSG deficit to be charged to an unusable reserve and held on the balance sheet, and hence the in year deficit on the DSG – which is a forecast cumulative deficit by March 2025 of £196m, is not included in the reported position.

63. The forecast position on the DSG is that by the end of March 2026, there will be cumulative deficit of £287m, and an ongoing annual deficit of circa £100m.

64. The position on DSG (as with the General Fund) is not sustainable, but as at the time of writing there has been no indication from the Government as to what will happen post March 2026 (although some additional one off funding of £1bn was announced in the Autumn budget). Further detail on the DSG position is set in section H.

Section H – Autumn Budget Statement

65. Prior to the budget announcement the Secretary of State for Local Government and English Devolution had set out on the 28 October in a Commons debate that the government '*would focus on aligning funding with deprivation levels, through an "initial rescue operation" in this year's financial settlement*'.

66. From a County Council perspective, the budget announcement was very disappointing; the budget offered little in terms of additional funding (best estimate is additional funding of £8.7m as set out below), and is far from a 'rescue package', leaving the council with a significant forecast budget shortfall for 2025/26 as set out above.

<u>Funding</u>

67. In her budget statement and as set out in the 'Autumn Budget 2024 – Fixing the Foundations to Deliver Change' budget book (Autumn Budget Book 2024), the Chancellor made the following high level commitments in terms of additional funding for upper tier Local Government :

    - **Adult Social Care**: £600m additional grant. If Hampshire receives a proportionate share in line with previous years, we could anticipate additional funding of £8.7m for 2025/26.
    - **SEN High Needs:** £1bn one off for Special Educational Needs and Disabilities (SEND) within the Core Schools budget; Hampshire's proportionate share would be around £15m to £20m based on past allocations; This has no impact on the General Fund position for 2025/26, and has been announced as one off funding pending a review of SEND provision in the spring (see paragraphs 87-93 for further analysis of the DSG position). There is some doubt as to whether this is entirely new money.
    - **Roads:** £500m via Department for Transport assumed to be ringfenced for local roads maintenance funding in order to go *"beyond the government's promise to fix an additional 1 million potholes per year"* (this is not included in the £1.3bn increase referenced below).

68. In terms of the overall Local Government Settlement (LGFS), the Chancellor set out an increase in funding of £1.3bn to local government for 2025/26 (excluding the £500m for roads), which together with an assumed council tax rise of 5% would provide for an increase in core spending power of 3.2%. The £1.3bn is inclusive of the £600m announced for social care, which leaves a further £700m of what is described as 'un-ringfenced grant'.

69. The budget announcement also set out that the government was committed to '*reform of the approach to allocating funding through the LGFS, starting with a targeted approach to allocating additional funding in 2025-26';* given that it seems the additional funding will include an element of targeted funding towards areas of deprivation, it is not possible to determine what the council's share of the overall additional funding will be.

70. In a post budget letter from the Deputy Prime Minster and Secretary of State for Housing, Communities and Local Government to Council Leaders, it was confirmed that:

> *'After years of delaying much needed fair funding reform…….we will reform the approach to funding allocations within the Local Government Finance Settlement by redistributing funding to ensure that it reflects an up-to-date assessment of need and local resources. This will start with a* ***deprivation-based approach in 2025-26 with additional funding targeted to the places that need it most****.*
>
> *Broader redistribution of funding will follow through a multi-year settlement from 2026-27.'*

71. This approach has two potential significant impacts for Hampshire:
    i) historically a funding formula based on deprivation has not worked favourably for Hampshire; we are the 16th least deprived Upper Tier Authority in England (ranked out of 151 authorities)[1]
    ii) estimating what our share of the announced £1.3bn will be difficult as the proposal is to allocate on a targeted approach based on deprivation, at this stage therefore we are only working on the prudent assumption of £8.7m for social care grant.

72. The letter to Council Leaders also confirmed that the government will issue a 'local government finance policy statement' (LGF Policy Statement) in November, which will include further details for the 2025/26 settlement and the proposed multi-year settlements for 2026/27 onwards.

73. The Society of County Treasurers (SCT) technical support team have estimated how the overall increase in Core Spending Power would be achieved, and their analysis, to which we have added the potential HCC impact, is set out below. This is caveated as this has not been set out within the Autumn budget report, but nevertheless is a helpful analysis:

Funding Stream	£m	HCC Commentary	Assumed HCC Impact £M
New Social Care Grant	600	£8.7m estimated allocation	8.7
Disabled Facilities Grant (DFG)	86	Passthrough nil impact	0
Funding to cover increase in Employer	200	Estimated direct impact to HCC staff costs £10m. We do not believe the SCT analysis is correct	neutral

[1] Index of Multiple Deprivation (IMD) 2019

Funding Stream	£m	HCC Commentary	Assumed HCC Impact £M
NI Contributions (HCC Direct Staffing Impact)		as there is a sum of £4.745bn shown in the control totals for NI impact on public sector.	
Funding to cover increase in Employer NI Contributions – Impact on suppliers particularly Social Care Providers	0	There is no direct funding set aside in the announcement to account for the indirect impact to HCC as all suppliers are impacted and will seek to pass on their costs	Negative but unknown
1.7% CPI uplift on last year's Settlement Funding Assessment (SFA - mainly RSG)	282	We only receive around £60k in RSG so any impact is negligible	0
Potential balancing sum, allocation methodology not known	200	Unknown, but would be minimal given this sum could cover all Local Authorities	0
Sub Total and aligns with the £1.3bn additional funding announced	**1,368**		**8.7**
Average 4.3% increase on 24-25 council tax (as per OBR)	1,551	MTFS already assumes 5%	0
0.8% taxbase increase on 24-25 council tax (as per OBR)	289	MTFS already assumes 1% including second homes impact	0
Total = 3.2% Core Spending Power increase	**3,208**		**8.7**

74. If the above analysis is correct, then other than our share of the £600m Social Care grant, we would not expect to receive any significant additional funding based on the funding streams identified, as effectively the DFG, NI and SFA are either negligible or neutral. That would just leave a potential share of the £200m which SCT have presumed is the balancing sum, which is a very small sum to be distributed on an unknown basis, potentially across all tiers of local authorities.

75. Even if the above SCT analysis is not correct, we would only anticipate at most potentially receiving additional grant (over and above the £8.7m assumed for social care) in the low £m, not counting funding for Employers National Insurance which we are assuming at best will be neutral (for our direct employment costs).

Council Tax

76. The budget statement made no reference to council tax or changes to the referendum rules.

77. The OBR analysis for council tax sets out that their *'council tax forecast is informed by known referendum principles, announcements by councils, and examining trends in recent behaviour'*; the OBR assumption is for an average council tax increase of 4.8%.

78. Our current working assumption based on both the budget statement and the OBR analysis is that there are no proposals to raise the referendum limit. We would anticipate that this will be confirmed either way in the November Local Government Finance policy statement, but we assume no change.

Increased Costs

79. The Chancellor also set a number of announcements which impact our costs:
    - increases to employer national insurance
    - increase to the National Living Wage

80. **Employer National Insurance (ENI)**: the following changes to employer national insurance contributions were announced as set out below:
    - an increase of 1.2% to the employer rate
    - cut the secondary threshold to £5,000

81. For our direct employment costs, it is understood that MHCLG have confirmed in a briefing to the County Councils Network (CCN) that this new burden cost to Local Government will be fully funded as part of the local government finance settlement, so the impact in terms of this update to the MTFS is deemed to be at best neutral and net nil. Funding of £4.745bn has been set aside for the public sector, but there is still the risk that the distribution of this will leave us with a shortfall.

82. However, of particular concern is that although this ENI increase will also flow through to all our external suppliers, and will be particularly impactful to our social care providers, there is no specific funding set aside for this in the budget announcement.

83. It is likely that providers will want to pass on their increased employment costs, and there is no new funding for this outside of the overall £1.3bn announced, so effectively an unfunded pressure.

84. **National Living Wage (NLW) –** this will rise by 6.7%, from £11.44 to £12.21 from April 2025. For 18 to 20-year-olds, the minimum wage will rise by 16% from £8.60 to £10, and for apprentices, the minimum wage will rise from £6.40 to £7.55 (up 18%).

85. Unlike the increase to ENI, CCN have been briefed that there is no additional funding for local government to specifically compensate for this increase.

86. The impact is twofold:

- This will increase our employment costs for individuals currently employed on Grade A, although this is quite a small cohort in overall terms.
- The more worrying impact from a cost perspective is that just like the ENI increase, this will feed through to all suppliers, but crucially will impact our adult and children's social care provider costs, who will look to pass this on in their contract prices. This will be a further pressure which is likely to feed through which is unfunded, but is very difficult to predict at this point.

Dedicated Schools Grant

87. The budget announcement included extra one off funding of £1bn for SEND and alternative provision for 2025/26, equivalent to 6% real growth; however, this has to be seen in the context that the national DSG deficit for the High Needs block (which encompasses SEND) is currently forecast by the County Council's network to be £4bn by the end the 2024/25 financial year.

88. In the budget the Chancellor referred to the £1bn as *'phase 1 of the spending review',* and that as part of a 'phase 2 spending review in Spring 2025', there would be **'***Further work to improve outcomes and return the system to financial sustainability***'**

89. The OBR set out in their analysis of the budget 'Economic and Fiscal Outlook October 2024' (Economic and fiscal outlook) that 'total local authority spending on SEND has doubled from £4.6 billion in 2017-18 to £9.0 billion in 2022-23'.

90. The OBR further comment that:

'Despite this short-term increase of central government funding there are still significant risks in relation to local authority finances and SEND. The current statutory override is due to end after 2025-26. If this happens and SEND spending needs continue to outpace central government grant funding, then some local authorities may be placed in financial distress or be unable to set balanced budgets from 2026-27 onwards.

In addition, the cumulative DSG deficits to date would then need to be recognised on local authority balance sheets which would create additional financial pressures – the DfE estimates that a third of local authorities will have cumulative deficits exceeding their reserves in March 2026'

91. There does not appear to be an easy solution to the DSG issues. Either:

- the statutory override is extended, which would be unsatisfactory and add further risk as it would just push resolution to a later year, whilst at the same time the underlying deficit would continue to grow; even if only extended by one year, Hampshire's forecast cumulative deficit would rise to circa £0.5bn by March 2027, which is clearly an untenable position for Hampshire to manage locally.

or

- the government commit to fully funding both the cumulative deficit and the ongoing annual shortfall; given the current financial climate, this option, whilst the most desirable, seems somewhat unlikely.

92. The OBR analysis resonates with Hampshire's position on the DSG deficit, which is that should government choose to simply disapply the statutory override at the end of March 2026, but does not fund the deficit position, the County Council would almost certainly have to issue a S114 notice at that point, as it would have insufficient reserves to fund the cumulative deficit nor the funds available to address the in-year deficit for 2026/27.

93. However, even with the statutory override in place, the DSG deficit still impacts on the County Council in the current year and will continue to do so for as long as the DSG deficit remains unresolved by Government; the impact is felt in two ways:

- the deficit has a real cash impact, so there is a loss of investment income for funding the deficit; at current investment rates of circa 5%, the full year impact of carrying the forecast £196m deficit at the end of 2024/25 in 2025/26 will be lost investment income of £9.8m, and that position will worsen as the deficit increases during 2025/26
- as the deficit impacts cash, it reduces the council's overall cash balances which in turn impacts cash flow; as set in section I, this impact will force the Council to undertake borrowing to support the underlying financing of the capital programme much sooner than otherwise would be required, with new borrowing now forecast to be required at some point during 2026/27.

Section I - Forecast Budget Gap for 2025/26 and 2026/27

94. The Medium Term Financial Strategy update to Council in November 2023 set out the key areas of financial pressure and associated assumptions which contributed to a projected budget gap of £132m for 2025/26. This forecast had been in place since the finance settlement was announced back in December 2022. The following table provides a summary of the budgeting assumptions within the previous MTFS position for 2025/26:

Variable	2025/26 – 2026/27 budgeting assumption	Average % increase
Non-pay Inflation	£26m allocated to directorate budgets plus centrally held contingencies of £7.5m	2% average for expenditure and income
Pay inflation	£11.4m per year	3%
Interest rates	Weighted average investment rate 3.28% in 2025/26	3.28%
Adult's	£20m average annual growth and above inflation	5%

growth	price increases	
School Transport	£14.4m average annual growth and price increases	20%
Children Looked After	£16.2m average annual growth and price increases	9%
Council tax	£94m additional Council Tax income over two years including taxbase growth and increase in precept	4.99% annual increase in precept plus 0.75% taxbase growth
Business rates	£3.5m additional business rates and top up grant income per year	2%
Social Care Grant	£14m increase assumed for 2025/26 to offset additional pressures in school transport	16% in 2025/26 only

Update to Forecast budget gap

95. Over the past year, demand and price pressures have continued to grow within social care and school transport services at a significantly faster rate than was anticipated. The key drivers for these increases are discussed in detail below. Whilst traditionally, the County Council has assumed a consistent growth trend line for key service areas, it is becoming clear that the combined impact of demand and price increases is creating more of an exponential growth curve, which we must start to try to incorporate into future forecasts albeit that is much more difficult to model on a consistent basis.

96. The revised budget gap positions for 2025/26 and 2026/27 after accounting for the forecast future year pressures as at quarter two are set out below. The opening gap position for 2026/27 reflects the assumption of at least an additional £60m - £70m deficit that the Council faces each year as a result of baseline pressures across demand led services exceeding additional funding available to the Council, primarily through increases to Council Tax. The gap in 2026/27 widens following the revised forecasts outlined in this report.

	2025/26 £m	**2026/27 £m**
Opening budget gap position per November 2023 MTFS	**132.0**	**192.0**
School Transport	19.3	24.8
Children Look After - Unaccompanied Asylum Seeking Children	6.3	7.6
Children's Social Workers	5.0	5.3
DSG Central School Services Block	1.5	1.5
Adult's Care Packages	16.7	27.8
Non-pay inflation	4.7	8.0

2024/25 local government pay offer	1.2	1.2
Debt financing and interest income	11.0	14.6
Removal of social care grant assumption	14.0	14.0
Removal of allowance for non-delivery of savings	(7.5)	(9.0)
Other miscellaneous updates – mainly a review of contingencies	(3.9)	(7.5)
Removal of annual reserve top ups	(2.9)	(2.9)
Council tax and business rates changes including business rate pool	(6.5)	(2.3)
Revised budget gap before savings and social care grant	**190.9**	**275.1**
Expected additional social care grant	(8.7)	(8.7)
Revised budget gap before savings	**182.2**	**266.4**
Original SP25 savings	(75.1)	(90.4)
Less changes to proposals agreed by October Cabinet	5.1	2.9
Less other changes to profiling and deliverability per Q2 monitoring report	4.0	6.4
Revised SP25 savings	**(66.0)**	**(81.1)**
Revised budget gap after agreed SP25 savings	**116.2**	**185.3**

97. The revised budget gaps after allowing for social care grant and before accounting for SP25 savings have increased by £50.2m and £74.4m in 2025/26 and 2026/27 respectively. The most significant contributing factor is the worsening position for School Transport with forecast growth and price increases having more than doubled over the past year.

Demand Pressures

98. The revised forecasts for School Transport, Adult's and Children's Social Care and Children's Social Work are supported by demand models that are reviewed on a quarterly basis and refined using the most recent possible data and assumptions. The models are also tested with prior years data to assess their ability to predict known results.

99. It is likely that the above forecasts will continue to move as the detailed budget preparation process is undertaken during Quarter 3. A further update on the future years financial position will therefore be provided to Cabinet as part of the December provisional cash limits report, but the key elements impacting on the forecast are detailed below.

Adult Social Care

Adult Care Packages

100. As set out in table above, since the last update to the MTFS, there is a further pressure of £16.7m forecast for 2025/26 for Adults Care packages.

101. The pressures seen within Older Adults are attributable to a steady acceleration in the growth of numbers of clients within Residential and Nursing Care since the pandemic following the recovery of the care market and increasing numbers of hospital discharges resulting in long term care.

102. It had been assumed that pressure on the local NHS would begin to ease following the end of the tail of COVID demand, but this has not transpired and sustained pressure on the health service continues to drive demand into older adult's long term care.

103. Throughout 2023/24 and 2024/25, Younger Adults Care has become an area of increasing concern. In 2022/23 around 70% of client growth was within Older Adults but as of the current financial year, more than half of the total financial pressure is within Younger Adults. We have seen growing numbers of young adults with significant mental health needs, many of whom are coming into social care in a position of crisis which has resulted in an increasing number of very high cost placements. As of March 2022 there were 52 younger adults placements costing over £3,000 per week, with a combined annual cost of £10.8m. As of quarter 2 this year there were 108 such placements with a combined annual cost of £29m.

Children's Services

School Transport

104. The unprecedented and sustained pressures facing the School Transport service have been widely reported by the Council (and across the country) and are central to our continued lobbying of government for funding and legislative reform. The cost of providing School Transport has risen rapidly since 2021/22 due to increased complexity of pupil needs, shortages of appropriate transport and the lack of locally available, suitable Special Educational Needs places.

105. A pressure of £21m is forecast for 2024/25 as reported in the Quarter 2 Financial Monitoring Report, representing a cost increase of around 29% since 2023/24. The 2024/25 MTFS highlighted School Transport as the single biggest risk to the Council's financial position to 2025/26 and this was confirmed in a recent review of the School Transport forecast, which identified a further shortall of £19.3m in the transport budget for 2025/26.

106. The majority of this pressure relates to the SEN cohort due to the increasing number of children with Education Health and Care Plans and shortages of dedicated SEN school places, resulting in longer journeys to schools which are further away. Market based factors also contribute significantly to the pressure; there is a lack of capacity in the transport provider market which drives up prices

due to lack of competition. This is exacerbated by increasing complexity of pupil needs, which means that children are more likely to require adapted vehicles or Passenger Assistants. The increased cost of Passenger Assistants comprises £1.3m of the total £24.8m transport pressure in 2026/27.

Childrens Social Care

107. The primary driver of pressures in Children's Social Care remains the exceptionally high cost of out of county residential placements which is driven by a lack of sufficiency and choice. These placements cost the council an average of £356,000 per year, so a small movement in placement numbers can significantly impact the forecast and this remains a key caveat to the revised gap position. The £6m additional pressure within Children's Social Care for 2025/26 is attributable to the changing age profile of Unaccompanied Asylum Seeking Children (UASC) in the Council's care.

108. The grant provided by government to cover the costs of providing care for UASC is paid at a flat rate per child. This is despite the higher cost of providing care to older children, which exceeds the per child allocation. In prior years, this shortfall has been offset by the lower cost of care packages for younger children. However, as the average age of the UASC cohort has increased, there is no longer flexibility to absorb the grant shortfall for older children and a substantial pressure has arisen which can only be addressed through an increase to the grant funding for UASC. The County Council continues to work with sector representatives to lobby government for a funding settlement that takes full account of the costs to local authorities of providing care to UASC, particularly once they become adults, where the Council still has a duty to provide support up to the age of 25. Given the nature of these clients, their support needs are often significant.

Children's Social Workers

109. There continues to be considerable growth in demand for Children Social Care, both nationally and locally. Accordingly, to maintain a safe level of provision, significant investment in social work staffing has been required, totalling over £20m since 2021/22. There isn't any sign that this growth trend is likely to slow down in the near future.

110. Accordingly, the Social Work staffing establishment has recently been modelled to take account of the likely level of growth and the staffing resources required to meet this projected need. Furthermore, there continues to be a shortage of experienced qualified Social Workers which is leading to greater reliance on agency staff to fill the volume of qualified posts required, a factor which is reflected in the latest staffing model.

111. The current projections for the staffing cohort required in Childrens Social Care, at the agreed safe caseload levels of no more than 20 cases per qualified Social Worker (agreed by County Council in 2017/18), indicates that by 2025/26

investment of a further £5.0m above the funding already built into the current MTFS will be required.

DSG Central School Services Block

112. The Central School Services Block (CSSB) of the Dedicated Schools Grant provides funding for local authorities to carry out central functions on behalf of maintained schools and academies. The pressure on the CSSB primarily relates to inclusion and support services, which have previously been funded by the one-off Supporting Families Grant. Legislation introduced in August 2024 which aims to improve school attendance has also extended the statutory duties of local authorities in this area. Additionally, the CSSB funds enabling services for schools including data and information, finance and property services which are also facing inflationary and growth pressures.

Inflationary Pressures

113. The central contingencies budget has included additional allowances for inflation in recent years, however forecast inflationary pressures across both pay and non-pay budgets continue to outstrip the funding available. Local government pay awards have increased significantly since 2021/22, reflecting higher rates of general inflation and increases to the National Living Wage of almost 10% per year. The 2024/25 agreed pay award averages 3.9% across all staffing grades, exceeding the budgeted level of 3%.

114. Within non-pay budgets, pressures have been driven by index linked increases to key contracts, including streetlighting, waste and highway maintenance, and increases to the National Living Wage have impacted the costs borne by external providers. Additionally, the publication of the results of the Fair Cost of Care exercise undertaken in 2022 has driven market expectations of the rates that local authorities should pay for Adult Social Care, further impacting prices.

115. There will potentially be a further unbudgeted inflationary impact as a result of the budget announcement increasing Employers National Insurance; whilst we should receive additional funding to offset the direct impact on our own employment costs, there is no additional funding to support the increased costs which our suppliers face, which many, particular social care providers may look to pass on to the County Council.

Interest on Balances/Requirement to Borrow

116. The MTFS position includes a significant reduction to the expected interest income achievable on cash balances held by the Council. The revised forecast takes account of the Council's worsening financial position and the resulting impact on cash balances as reserves are utilised to bridge recurrent shortfalls in the revenue budget. The use of reserves for this purpose is expected to accelerate over the coming years as the budget deficit grows, potentially requiring the Council to take out additional external borrowing by 2026/27 to maintain

adequate cash balances throughout the year, a position which the Council has not faced for over a decade.

117. As set out in paragraph 93, the continued and growing DSG deficit is significantly impacting cash balances, and will be the main reason why the council is forecast to need to borrow in 2026/27, much earlier than otherwise would be the case.

118. There is potentially a technical issue to resolve with MHCLG and CIPFA, in that a council is only allowed to borrow to fund its capital financing requirement (CFR), which reflects the borrowing required to fund the capital programme; technically the forecast requirement to borrow in 2026/27 is driven by cash balances being reduced by DSG to the extent that the actual borrowing would exceed the borrowing required solely to fund the capital programme.

119. This position would be problematic as the technical accounting rules governing borrowing do not permit borrowing to fund revenue expenditure (except where a council has a capitalisation direction in specific circumstances or is in receipt of Exceptional Finance Support from Government).

120. However, given the unique circumstance which a borrowing requirement attributable to an underlying DSG would present, we anticipate that borrowing would be permissible through agreement with Government. As there was no resolution to the DSG issue in the October budget, officers will raise this issue with both MHCLG and CIPFA

Council Tax and Business Rates

Business Rates Pool

121. The Chief Financial Officer (CFO) has reviewed the opportunity of the County Council entering into a Hampshire Business Rates Pool (BRP) and has concluded that creating a BRP for the 2025/26 financial year could offer a significant one-off financial benefit and is recommending as part of this report that the County Council commits to joining the proposed Hampshire BRP for 2025/26. The pool will encompass the County Council and five district councils: East Hampshire, Gosport, Havant, Test Valley, and Winchester.

122. Lower tier and unitary authorities pay a levy on any business rates growth above their spending baselines, which are set by government. A business rates pool combines the business rates income and spending baselines for the participating authorities, resulting in a net levy which is lower than that for the individual pool members if they remained outside the pool. The overall financial benefit of the proposed pool has been estimated at around £9m, of which HCC will receive a 50% share with the five districts splitting the remaining 50%.

Council Tax Premium Second Homes

123. Government has provided local authorities with the option to charge homeowners twice the normal rate of Council Tax on second properties from 1st April 2025. Several of the Hampshire District Authorities have opted to introduce a Council Tax premium on second homes in 2025/26.

124. A prudent estimate of the County Council's share of the additional Council Tax income expected has been included in the revised gap position, which is equivalent to a quarter percentage point increase in the taxbase. An updated estimate of the 2025/26 taxbase will be included in the final budget for approval by Cabinet and Council in February.

Section J: SP25 Savings Programme

125. The original savings proposed and agreed for SP25 totalled £90.4m of which £17.494m of which were subject to Stage 2 consultations.

126. These consultations have now concluded and Cabinet confirmed at its meeting on the 14 October 2024 to take forward savings of £14.631m.

127. The current position for SP25, as set out in the table below, is that the total savings now anticipated to be delivered for SP25 is £84.2m; this takes account of some savings now deemed undeliverable:

		£m
Baseline target		**90.4**
Undeliverable savings	(3.3)	
October Cabinet decisions – consultation items	(2.9)	
Total changes to SP25 Phase 1 Savings	***(6.2)***	
Revised baseline – SP25 Phase 1 Savings		**84.2**

128. Further detail on the above changes against the baseline target are set out in Quarter 2 Monitoring report elsewhere on the Cabinet agenda.

SP25 Phase 2 Savings Programme

129. Officers have been working on a further set of savings (SP25 Phase 2), based on the County Council returning to its 'core purpose' and considering what further savings could be made if we delivered services at the legal minimum service level.

130. Directors, supported by an Independent Panel have already been working on the development of these new proposals for consideration as part of the budget setting process and this work has looked at further Directorate opportunities for savings, new or extended areas for income generation and opportunities for cross cutting savings.

131. The forecast budget gap for 2025/26 net of an assumption that the available sum of £91.925m in the BBR is used to support the budget, is £24.275m:

	2025/26 £m	**2026/27 £M**
Gross Budget Deficit	182.2	266.4
Less SP25 Phase 1 Savings	(66.0)	(81.1)
Net Recurring Budget Gap	**116.2**	**185.3**
Apply BBR	**(91.925)**	
Revised Budget Gap	**24.275**	**185.3**

132. Whilst the LMSL work is still in progress, there is a level of confidence that the outcome will be an identification of additional SP25 Phase 2 savings of at least £24.3m, which would allow the budget to be balanced for 2025/26, if that was the only option employed to close the remaining budget gap.

133. Once finalised the SP25 Phase 2 savings will be brought forward for consideration by Cabinet as part of the lead into the budget setting report for February 2025, with the proposals to be considered by Select Committees during January 2025.

134. The current progress with the identification of these new savings through the LMSL work, whilst making excellent progress, makes it clear that balancing the remaining forecast budget gap of £116.2m (net of SP25 Phase 1 savings) through additional recurring SP25 Phase 2 savings will not be possible.

135. As set out in section L, it is therefore anticipated that Cabinet and ultimately Full Council, will need to consider and implement other options in order to balance the 2025/26 budget.

Section K: SP25 Phase 3 Savings Programme

136. In addition to the work set out above on bringing forward savings as part of SP25 Phase 2, for inclusion in the February budget report, there is further work in train on savings options which need further development, primarily arising out of the LMSL work and in particular, the positive challenge provided by the Independent Panel. These are referred to as SP25 Phase 3 savings.

137. These potential savings options will take time to develop (for example where a proposal could significantly impact existing service operating models) which means that it is unlikely these options will have been worked up in time for inclusion as fully costed savings proposals as part of the savings recommended to Cabinet as part of the February budget report; to be clear these potential

additional savings are not included in the SP25 Phase 2 work in progress savings highlighted above.

138. These Phase 3 savings will therefore need to come forward post February 2025, to allow the time needed to fully develop the proposals, but any achievement during the year would clearly be a bonus.

Section L: Options for Closing the Budget Gap

139. Taking into account the in-year forecast position, the anticipated growth in adults' and children's social care and home to school transport and all the other budget pressures we face, and the relatively small increase in funding we anticipate following the budget announcement, the revised MTFS forecast shows a gross recurring deficit of £182.2m for 2025/26 rising to £266.4m for 2026/27.

140. As set out in section I, **the net forecast gap for 2025/26 is £116.2m** (£185.3m 2026/27), which is net of the impact of the £84.2m SP25 savings already agreed (of which £66m is delivered in 2025/26, and £81.1m in 2026/27), and before assuming any draw from the BBR:

	2025/26 **£m**	**2026/27** **£M**
Gross Budget Deficit	182.2	266.4
Less SP25 Phase 1 Savings	(66.0)	(81.1)
Net Recurring Budget Gap before any assumption about drawing from the BBR	**116.2**	**185.3**

141. Given the size of the net budget gap at £116.2m, for 2025/26, which is after accounting for SP25 phase 1 savings, **it is clear that as signposted and anticipated for some time, the County Council has reached the point where it is unable to find the level of savings required to balance the budget on a recurring and sustainable basis**.

142. The position not surprisingly worsens for 2026/27, where the net gap after agreed SP25 phase 1 savings is £185.3m.

143. It remains the case that if there is:

- no further announcements around legislative change or freedoms and flexibilities, and/or

- no significant increase to the funding the Council receives (particularly on the back of the spending review next year which the government have set out will include broader redistribution of funding through a multi-year settlement from 2026/27) and/or

- no change to the allowable council tax increase for either 2025/26 or 2026/27,

144. **Then it is pretty clear that the County Council would need to issue a Section 114 notice for 2026/27**.

145. In the short term, the council will need to look at all available options for balancing the 2025/26 budget, to ensure that a S114 notice is avoided for next year, as this will at least allow the council to consider the outcome from the review of the local government funding formula and the introduction of 3 year settlements.

146. Whilst there is the option of substantially closing the budget gap through an unplanned draw from reserves through use of the BBR, this would pretty much mean utilising all spare resources available, and seriously depleting financial resilience. It would leave the Council with very little wriggle room, and all other things being equal and no change in our funding position, would make the prospect of issuing a Section 114 notice almost an inevitability for 2026/27.

147. It is therefore imperative that Cabinet and Full Council consider the full range of options available to balance the 2025/26 budget in order to minimise the use of reserves, and the options which potentially could be considered include:

    - **Further lobbying** - to seek change either as part of the November Policy Statement or within the Provisional Local Government Finance settlement in December. This will include legislative change to decrease demand, freedoms and flexibilities on charging and levels of council tax increase.
    - **Exceptional Finance Support** – If the above changes are not forthcoming, to open discussions with the Government on seeking Exceptional Finance Support (EFS) for 2025/26, such support to be by allowing the Council to raise council tax above the 5% referendum limit but without recourse to a referendum (this approach has been allowed in other financially stressed authorities). Hampshire is the second lowest County Council Tax and an increase to bring us up to an average level could be agreed and could be worth over £45m.
    - **Council Tax Referendum** - if the option of EFS is not agreed by government, there remains an option to propose a council tax rise above 5%, and to seek a referendum to be conducted in May 2025.

148. The options are not mutually exclusive, as a mix of a one off draw from reserves could be utilised (albeit the preference would be to limit the use of reserves) alongside either EFS or a council tax referendum. Further detail on the above options for closing the budget shortfall are set out below.

Draw from Reserves

149. In anticipation of there being a significant budget shortfall for 2025/26 and beyond, the CFO has undertaken a forensic and detailed review of both Reserves and the Capital Programme, to free up additional revenue resources to help balance the budget on a temporary basis.

150. Through this work, total revenue resources of £108.715m have been identified which can be repurposed, of which £64.9m has been re-purposed to the Budget Bridging Reserve, which increases total amount in the BBR to £91.925m; this sum is available as an option to support setting the 2025/26 budget.

151. However, in reaching this point the council has significantly reduced its available usable revenue reserve, and this will significantly limit the Council's opportunity to utilise reserves in future and is not in any way a sensible or sustainable way to manages the finances of an organisation which spends over £2.5bn every year.

152. It also means that overall financial resilience is reduced, which just adds further risk to a challenging financial position.

153. If the budget was partly balanced through fully drawing down the sum of £91.925m from the BBR, this would take the cumulative draw since 2022/23 to £254.83m; the draw has increased each year, significantly depleting reserves, and is not sustainable:

	Draw from BBR to Balance the Budget **£M**
2022/23	38.00
2023/24	50.80
2024/25	74.10
2025/26	**91.93**
Total Draw	**254.83**

154. Given the significant revenue sums repurposed from capital and reserves to support the 2025/26 budget, usable reserves are significantly depleted. The analysis at Appendix 4 shows what the reserves position will be following the transfers and highlights that most of the remaining reserves (86%) are fully committed leaving only £60.6m uncommitted albeit over half of this is to offset risk. This is in stark contrast to a forecast deficit of £287m on DSG by the end of

March 2026. Whilst the General Fund Reserve is technically not committed, any use of the reserve must be replaced in future years.

155. Given the above position on reserves and the size of the forecast budget gap in 2026/27, it is unlikely that there would be sufficient reserves (save for undertaking a significant level of borrowing to support the capital programme) to balance the 2026/27 budget on a one off basis, hence why all other things being equal, the likelihood that the council would issue a S114 notice is on balance more likely than not.

156. Further details on the review of the capital programme and reserves is set out in Section M.

Exceptional Finance Support

157. Since 2020, the government has agreed to provide a number of local authorities with support via the Exceptional Financial Support framework, following requests from these councils for assistance to manage financial pressures that they considered unmanageable.

158. In all cases, the government has set a clear expectation that the authorities continue to manage and mitigate their financial pressures, as well as respond effectively to the individual challenges they are facing and provide regular updates to the government on progress.

159. The support is provided on an exceptional basis, and on the condition that each local authority is subject to an external assurance review.

160. Whilst support provided via this framework is usually provided in the form of a capitalisation direction (capitalisation directions permit a local authority to meet revenue costs through capital resources), a number of Council's have requested, and been allowed to implement without recourse to a referendum, an above referendum limit (which is 5%) council tax increase.

161. A Capitalisation Direction granted through EFS typically has the following characteristics:

- it allows borrowing or the use of capital receipts to fund the revenue budget shortfall for any agreed financial year
- effectively if borrowing is utilised to fund a revenue shortfall, it will add borrowing costs of both MRP and interest for some time into the future; the capitalisation regs require a 20 year payback of borrowing (if we borrowed to fund the forecast gap to avoid depleting reserves, we would need to borrow around £91m. Assuming current interest rates for borrowing, if we borrowed that sum over 20 years it would add a cost of around £9m per year)
- and that would need to be repeated each year a Capitalisation direction was required

- the underlying assumption is that an Authority granted a Capitalisation Direction will be able to find sufficient savings to close its budget gap including the additional borrowing costs

162. Given the detailed work we have undertaken to review all services against our Core Purpose and to establish services at their Legal Minimum Service Levels, we do not believe that EFS in the form of a capitalisation direction is a sensible option, as we do not believe that the Council can make the level of savings required to balance the budget in 2025/26 or 2026/27 (a position supported by the Independent Panel).

163. That being the case, a Capitalisation Direction merely adds cost through borrowing (we don't have sufficient capital receipts to fund a capitalisation direction), and only provides a temporary sticking plaster to an underlying long term problem for which we do not believe can be addressed through sufficient recurrent additional savings.

164. **To be clear, if entering discussions on EFS, we would not be seeking a Capitalisation Direction for the reasons set out above.**

165. However, it would make sense to discuss EFS with government in the context of that EFS support allowing the Council to implement an above referendum limit council tax increase.

166. For example, for 2024/25 the following authorities were granted permission to implement an above referendum limit council tax rise without recourse to a referendum:

Authority	**Council Tax Increase 2024/25**
Woking District Council	10.00%
Birmingham City Council	9.99%
Slough Unitary Authority	8.50%
Thurrock Unitary Authority	7.99%

167. The allowance of an above referendum limit increase has usually only been granted where an authority is already subject to some form of government intervention, and the government have rejected requests from a number of authorities to allow an above referendum increase even though it would be a clear and obvious way for an authority to reset its financial position and avoid the potential of having to issue a S114 notice.

168. Nevertheless, it is clearly an option we should discuss with government given our current and forecast financial position; thus far the government have focused on

whether a council is able to set its upcoming budget (for example through the use of reserves), rather than having concern for the underlying recurring revenue shortfall and the sustainability of a council beyond a one year time horizon. Where a council can survive its next budget year there has seemingly been a reluctance to acknowledge the underlying position and to enter into any meaningful discussion with an authority who believe they are in financial difficulty.

169. That being said, in a recent communication from MHCLG to council Chief Financial Officers on the 1st October 2024, the government set out the following:

> *'as part of this engagement, a small number of councils have asked for clarity on the future support process if it is not possible for them to set a balanced budget. Ministers are clear that any council with concerns about its ability to set or maintain a balanced budget should approach the Department to discuss its position.* ***I wanted to confirm now that MHCLG will continue to operate a process to support councils in the most difficult positions. It remains the case, however, that Ministers will expect councils to have taken all reasonable action at a local level and that requests for support will be agreed on an exceptional basis.***
>
> *While government will continue to expect councils to make sure they are doing all they can locally to deliver for residents, Ministers are clear that this process will be collaborative and supportive of councils. We will, as ever, treat all discussions in confidence.'*

170. It is proposed that the Leader, Chief Executive and CFO engage with MHCLG to discuss our underlying financial position and to discuss the opportunity of EFS through an above referendum limit council tax rise.

<u>Council Tax Referendum</u>

171. There is the option of proposing a council tax rise above the referendum limit of 5% if the government do not grant this via a request for EFS, which would then require the council to propose and hold a referendum.

172. To be worthwhile in terms of going through the referendum process, a referendum would only really be worth proposing if the council tax increase proposed was significantly above the referendum limit, as this would ensure both a worthwhile benefit in year for 2025/26, but would also be built into the council tax base for all later years so would have a compounding beneficial effect for all later years.

173. Each additional 1% is worth around £8.2m, so for example a 15% increase would yield an additional £82m. At 15% the 2025/26 budget shortfall would be substantially closed with only a small one off draw from the BBR required to balance the budget, and this would also significantly reduce the 2026/27 budget gap.

174. The date for holding the referendum must be no later than the first Thursday in May. Responsibility for organising a council tax referendum lies with Hampshire's

billing authorities (the District Councils). They must organise referendums on the County Council's behalf.

175. The County Council would start the process by publishing an initial notice stating that a referendum is to take place. It must do so as soon as reasonably practicable after determining that its council tax increase is excessive (likely to be at the Council meeting where the Council Tax is set) and not less than 28 days before the poll.

176. This should set out, amongst other things, the reason for the referendum, the referendum question (the question format being set out in Regulations), the authority that will organise the referendum and where further information about the referendum can be obtained. This notice triggers the period during which the referendum campaign expenses limit will apply.

177. The Council must also publish on its website, and possibly elsewhere, information about the costs of the referendum (both estimated and, later, final costs).

178. The Council may also publish a statement setting out its reasons for the council tax increase and the likely consequences if it is not approved.

179. The costs of holding a referendum would fall to the County Council and the District Councils would be entitled to recover the expenses incurred in holding a referendum on its behalf. However, where the polls for a referendum are combined with those for any other election, the cost of taking the combined polls (excluding any cost solely attributable to one election or referendum) and any cost attributable to their combination would be apportioned equally among the elections or referendums.

180. As there will be County Council elections in May 2025, the costs of holding a council tax referendum would be significantly minimised and there are also District Council elections in most areas in May 2026, which would also provide an opportunity to reduce the costs of a referendum.

SP25 Phase 3 Savings

181. In addition to the above options, the council will continue to review all options for delivering additional savings, and as set out in section K there are a number of additional options being developed.

Section M: Review of the Capital Programme and Reserves

Review of capital programme

182. Capital expenditure involves expenditure to create or enhance assets to support the delivery of services. Expenditure varies from year to year but is typically around £200m. A significant proportion is funded from external sources, including government grants and developer contributions (2023/24: 88%). This is however supplemented using capital receipts and internal revenue resources where necessary.

183. The use of revenue resources to support the investment in capital assets impacts the revenue budget in one of three ways:

- A reduction in existing reserves
- Borrowing costs
- Direct contributions from the revenue budget.

184. Balancing the need for capital expenditure with the affordability of the capital programme has always been a priority – and is a key consideration in complying with the CIPFA Prudential Code.

185. Given the increasingly challenging financial environment all revenue-based spending is being reviewed and challenged as part of the work on legal minimum service levels. This includes the use of revenue resources to fund the capital programme.

186. In reviewing the programme, the aims have been threefold:

- to be able to make ongoing savings from the revenue budget through reduced annual contributions to capital and/or lower prudential borrowing costs
- to release existing funding earmarked within the capital payments reserve which could then be transferred to the budget bridging reserve
- to continue to invest in capital assets where it is appropriate to do so in the context of LMSL and the Prudential Code

187. Reviewing projects and priorities across the capital programme has identified a number of opportunities to release revenue funding from the Capital Payments Reserve of £38.257m by removing projects where the expenditure is not considered essential in the context of LMSL and the overall financial position.

188. The proposed schemes and earmarked revenue funding it is recommend to remove from the capital programme is set out in the table below.

189. If the changes set out are approved by Cabinet and Full Council as part of this report, from the funding released of £38.257m, £28.257m will be added to the BBR, and £10m will be set aside as capital contingency, and the capital programme will be updated and re-presented to Full Council to reflect these changes in the next reporting cycle,

Proposed Projects/Earmarked Sums to remove from the Capital Programme

Existing allocation	Risk/impact of reallocating	£m
Inflation risk reserve – unallocated balance	Reduced flexibility to meet inflationary pressures.	4.101

Existing allocation	Risk/impact of reallocating	£m
Inflation risk reserve – net reduction in TCF allocation	Funding no longer required for the TCF programme. Release of £1.2m previously allocated less £0.45m reallocated to revenue costs of Junction Road scheme.	0.750
Market Town Fund	Additional funding may be requested in future	0.335
Flood and coastal defence	Priorities in this area are likely to arise in future needing funding	3.298
Investment in Hampshire	Impact on Hampshire organisations who would benefit from this grant funding	2.554
Advance and advantageous land	Borrowing can be considered if appropriate opportunities arise	2.989
Office accommodation and property fund	Funding may be required on an ad-hoc basis in future	3.413
Reallocation of alternative funding	No impact – availability of alternative funding to fund projects allows this funding to be released from the CPR	2.293
Universal Services contingency	Reduced ability to meet emerging pressures	2.511
Children's Services	Reduced ability to meet emerging pressures	2.244
Corporate balance[2] (primarily unallocated capital receipts)	Reduced ability to meet emerging pressures	13.664
Other allocations		0.104
Total		**38.257**

[2] This balance primarily relates to the benefit of capital receipts generated by the County Council. It is appropriate to release this balance as the additional capital receipts means this funding can be used for capital schemes in place of previously planned revenue contributions to capital, releasing the revenue based funding to the BBR.

190. The approach taken has been to review schemes against specific known needs. This does not mean there will not be future needs for expenditure it is simply that in the current financial environment it is considered that the best decision that can be made in the context of LMSL principles and the forecast budget gap is to add any balances not immediately required to the Budget Bridging Reserve.

191. This approach is not risk free and clearly will mean there is less flexibility in future to meet emerging capital priorities from existing resources, including priorities that arise in areas where earmarked funding is proposed to be released.

Schemes Funded By Prudential Borrowing

192. The review of schemes continues, with the remaining focus primarily on schemes due to be funded by prudential borrowing; removal of schemes funded by borrowing will benefit the revenue budget (lower interest and MRP costs) but this benefit will be felt over time, compared with the immediate benefit of releasing funding earmarked from reserves.

193. As part of this review, it is recommended that the allocation from prudential borrowing for strategic land purchases of £10m within the Hampshire 2050 capital programme is removed, with the resultant MRP and interest saving included within the capital financing costs included within the MTFS.

194. If potentially advantageous strategic land opportunities are identified in the future then a new addition to the capital programme will be required and the usual decision process will be followed subject to a business case.

195. A further update will be provided if additional opportunities are identified.

Manydown North

196. Members will be aware that following many years of complex negotiations and discussions, the Joint Venture limited liability partnership owned by Hampshire County Council (25%), Basingstoke and Deane Borough Council (BDBC – 25%) and Urban and Civic (our private sector partner who own 50%) completed on the purchase of land at Manydown North in Basingstoke and signed a series of documents that enable development to progress on the site.

197. The final days of the completion required a series of decisions to be made internally, some of which were delegated to the Director of Hampshire 2050 and some which had to be taken as urgent decisions by the Director of Corporate Operations in consultation with the Leader and the Chief Executive. These urgent decisions need to be reported to Cabinet and County Council at the next available opportunity.

198. The urgent financial decisions consisted of:

- £1.175m towards the purchase of a number of existing properties on the development together with liabilities for Stamp Duty Land Tax (SDLT).

- £1.15m for the Business Plan costs up until the end of November 2024 for the Manydown Development Vehicle LLP (the Joint Venture in which HCC owns a 25% share).

199. These costs represent Hampshire's 25% share of the overall costs incurred and approval to spend had to be in place at the point the various contracts were signed which is why an urgent decision under Financial Regulations was required. A total of £2.25m was included within the capital programme for these items and these approvals exceed that amount by £75,000.

200. There are however other sums in the capital programme for Manydown which were utilised on a temporary basis and this report seeks to re-instate that provision and approve further amounts that are required to progress the Manydown development for the remainder of the year (which runs until September 2025).

201. The further approvals that are required are:

- £0.075 addition to the capital programme to re-instate the provision for C and D loan notes associated with the final financial deal.

- £1.741m to cover other remaining items within the agreed business plan for the year, for which approval to spend is also sought.

- Approval to spend for the C and D Loan Notes totalling within the Capital Programme which will be drawn down (repaid, transferred or converted) in line with the agreed financial deal with Urban and Civic and Manydown 2018 Ltd (the original freehold owners of the site).

202. The additional total funding of £1.816m identified above will be met from the freed up capital resources identified above.

Review of reserves

203. An update on reserves balances was included in the end of year financial report in July 2024. The movement in reserves over the previous two financial years is summarised in the table below.

	31/03/2022	**Movement**	**31/03/2023**	**Movement**	**31/03/2024**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
County Council revenue reserves	598,888	(45,073)	553,815	(38,459)	515,356
EM3 LEP reserve *	3,741	(169)	3,572	269	3,841

Total County Council Useable Revenue Reserves	**602,629**	**(45,242)**	**557,387**	**(38,190)**	**519,197**
Schools reserves	83,903	(2,580)	81,323	5,494	86,817
Capital grants unapplied	196,447	9,845	206,292	21,037	227,329
Total reserves	**882,979**	**(37,977)**	**845,002**	**(11,659)**	**833,343**

204. The table shows that County Council useable revenue reserves fell by over £83m in the two years to 31 March 2024 (from £602.6m to £519.2m)

205. It is also worth noting that this table excludes the Dedicated Schools Grant (DSG) deficit (31/3/24: £123.9m) due to the statutory override put in place by central government.

206. The County Council holds reserves for a number of different purposes, as set out in the Reserves Strategy that forms part of the budget setting papers prior to each financial year.

207. A review of the existing useable reserves of £519.197m has been undertaken as part of the work in reviewing legal minimum service levels and supporting the County Council in remaining financially sustainable in the short term.

208. As has been said for many years, reserves can only be spent once and using reserves to bridge a budget gap without a sustainable solution to address the drivers of that gap is only a short term fix. However, in the context of the current environment and the principles of the work on legal minimum service levels, anything consistent with those principles to bridge a short term gap must be considered.

209. The review of useable reserves has identified a number of opportunities to release and repurpose existing earmarked reserves with the proposed additions and reductions to individual reserves set out in the table below.

Reserve	Impact	Reduction in reserve £m	Increase in reserve £m
Capital payments reserve (CPR)	The Table in paragraph 190 sets out the CPR allocations which it is proposed are removed and allocated to the BBR. It is however noted that releasing this funding (£38.5m) in full removes funding flexibility, so it is proposed that	(38.257)	

Reserve	Impact	Reduction in reserve £m	Increase in reserve £m
	£10m is held back as a central capital reserve		
Directorate and trading unit reserves	The review of Directorate reserves has enabled circa £25m to be released to the BBR; there is an acceptance that holding these reserves enabled Directorate's to manage issues locally, and that by releasing this sum there may be future unavoidable pressures for which corporate funding may be required	(24.928)	
Corporate cost of change (CoC)	A review of Directorate CoC reserves has enabled £25m to be released to the BBR reserve; all CoC is now held in a Corporate CoC reserve, with a remaining balance of £47.3m of which £30.5m is required to fund existing commitments.	(25.000)	
Insurance Reserve	This removes the provision within this reserve to cover the capital rebuild of a school; the reserve remains above the actuarially assessed suggested provision, and worse case the council still has recourse to borrowing for a major capital rebuild	(20.000)	
IT Reserve – Mobile Phone refresh	A full review of the allocation of mobile phones has been completed, which has reduced the allocation of smartphones by over 60%; this frees up resource of £0.530m as the 'released' smartphones will therefore not require replacement	(0.530)	
General Fund	As other balances reduce a greater general balance is required as risk mitigation. This addition will increase this reserve to circa 5% of net revenue budget		25.000

Reserve	Impact	Reduction in reserve £m	Increase in reserve £m
Budget Bridging Reserve (BBR)	This reserve was set up to provide one off reserve funds which could be used to balance a budget shortfall; allocating funds to the BBR provides additional one-off funding which could be used to support the setting of a balanced budget for 2025/26		64.899
Manydown Funding	Required funding as set out in paragraphs 197 - 203		1.816
Capital (RCCO) Contingency	As set out above in against the CPR reserve, it is proposed to retain a central capital contingency		10.000
Digital Optimisation	To ensure the Council can accelerate its implementation of digitally optimised solutions to drive out process efficiencies and cashable savings		2.000
Redundancy provision	A provision to cover potential redundancy costs		5.000
Total		**108.715**	**108.715**

210. Whilst the above table sets out a number of movements between reserves, the largest two movements are significant and important in terms of overall resilience:

- **General Fund:** the addition of £25m to the General Fund reserve increase this reserve to just over £50m, and as risk increases this provides an increased level of resilience, and puts the reserve in line with other Counties in terms of this reserve as a percentage of Net Revenue budget
- **BBR:** a significant addition of nearly £65m to the BBR reserve which will provide a potential source of funding on a one-off basis to support a balanced budget in 2025/26. The BBR in total is now just under £92m as set out in the following table:

	£m
BBR @ 31st March 2024	95.482
Draw to balance 2024/25 Budget	(74.133)
Revised position	**21.349**
Reduction to Insurance Reserve	20.000
Review of Capital and Reserves	44.899
Early delivery SP25 - Phase 1	20.686
2024/25 Forecast Outturn Pressure	(15.009)
Forecast BBR at 31 March 2025	**91.925**

REQUIRED CORPORATE AND LEGAL INFORMATION:

Links to the Strategic Plan

Hampshire maintains strong and sustainable economic growth and prosperity:	**Yes/~~No~~**
People in Hampshire live safe, healthy and independent lives:	**Yes/~~No~~**
People in Hampshire enjoy a rich and diverse environment:	**Yes/~~No~~**
People in Hampshire enjoy being part of strong, inclusive communities:	**Yes/~~No~~**

Other Significant Links

Links to previous Member decisions:	
Direct links to specific legislation or Government Directives	
<u>Title</u>	<u>Date</u>

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

<u>Document</u>	<u>Location</u>
None	

EQUALITIES IMPACT ASSESSMENT:

211. **Equality Duty**

The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited by or under the Act with regard to the protected characteristics as set out in section 4 of the Act (age, disability, gender reassignment, marriage and civil partnership, pregnancy and maternity, race, religion or belief, sex and sexual orientation);
- Advance equality of opportunity between persons who share a relevant protected characteristic within section 149(7) of the Act (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, sex and sexual orientation) and those who do not share it;
- Foster good relations between persons who share a relevant protected characteristic within section 149(7) of the Act (see above) and persons who do not share it.

Due regard in this context involves having due regard in particular to:

- The need to remove or minimise disadvantages suffered by persons sharing a relevant protected characteristic that are connected to that characteristic;
- Take steps to meet the needs of persons sharing a relevant protected characteristic that are different from the needs of persons who do not share it;
- Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity in which participation by such persons is disproportionally low.

212. **Equalities Impact Assessment:**

Given that this report deals with an update on the financial position of the County Council, no specific EIA has been undertaken, however as proposals under Phase 2 of the SP25 savings programme come forward they will be subject to the usual EIAs process and will be published with the final papers.