Sheffield City Region

COMBINED AUTHORITY

CA/LEP Revenue Budget Highlights

SCR Finance

22/03/2017

Summary

1. Summary
2. Reserves
3. Income
4. Expenditure
5. Sustainability Issues

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Executive Summary

Partner Contributions

- Subscriptions from local partners frozen at 2016/17 levels

On-going Pressures

- Further refinement to EZ business rate forecasts for 2017/18 means income is now c. £1m down on 2016/17 levels
- This pressure is partially mitigated through:
  - Release of reserves from prior year EZ corrections
  - Release of forecast underspend from 2016/17
  - Finance challenge on non-core spend

Service Impact

- Aspirations are being pared back to resource:
  - 26% of the establishment structure will be held vacant
  - Significant one-off costs are being managed from baseline development and marketing budgets
  - Capacity restrictions to taking on new activity

Sustainability

- Growth required in core activity income streams to maintain revenue spending power
- Future funding plan required for Access to Finance and Growth Hub teams

Partner Contributions

Frozen at 2016/17 levels

Base subscriptions have been frozen since 2013

	2017/18	2017/18	2017/18	2016/17	
	Base	Transport	Total	Total	Variance
Partner	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Barnsley	£32	£174	£206	206	£0
Bassetlaw	£4	£0	£4	4	£0
Bolsover	£4	£0	£4	4	£0
Chesterfield	£4	£0	£4	4	£0
Derbyshire Dales	£4	£0	£4	4	£0
Doncaster	£41	£222	£263	264	-£1
North East Derbyshire	£4	£0	£4	4	£0
Rotherham	£36	£190	£226	226	£0
Sheffield	£76	£415	£491	489	£2
	£205	**£1,000**	**£1,205**	**£1,205**	**£0**

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Income

- Close to £1m down on prior year
- Fall principally down to Enterprise Zone retained business rates, but also some reductions in sundry income

			2016/17	2017/18	Variance
			Budget	Forecast	
Forecasts	**Funder**	**Status**	**£'000**	**£'000**	**£'000**
Enterprise Zone Business Rates	Local Partners	Forecast	£2,724	£2,890	-£167
Adjustment for Prior Year Enterprise Zone Business Rates	Local Partners	Forecast	£319	-£711	£1,030
Total Enterprise Zone Business Rate Income	**Local Partners**	**Forecast**	**£3,043**	**£2,180**	**£863**
Local Authority Contributions	Local Partners	Committed	£1,204	£1,204	£0
LEP Grants	Government	Committed	£500	£500	£0
Investment Income	SCR	Forecast	£284	£195	£89
Traded Income	SYITA Properties	Committed	£20	£0	£20
			£5,051	**£4,079**	**£972**

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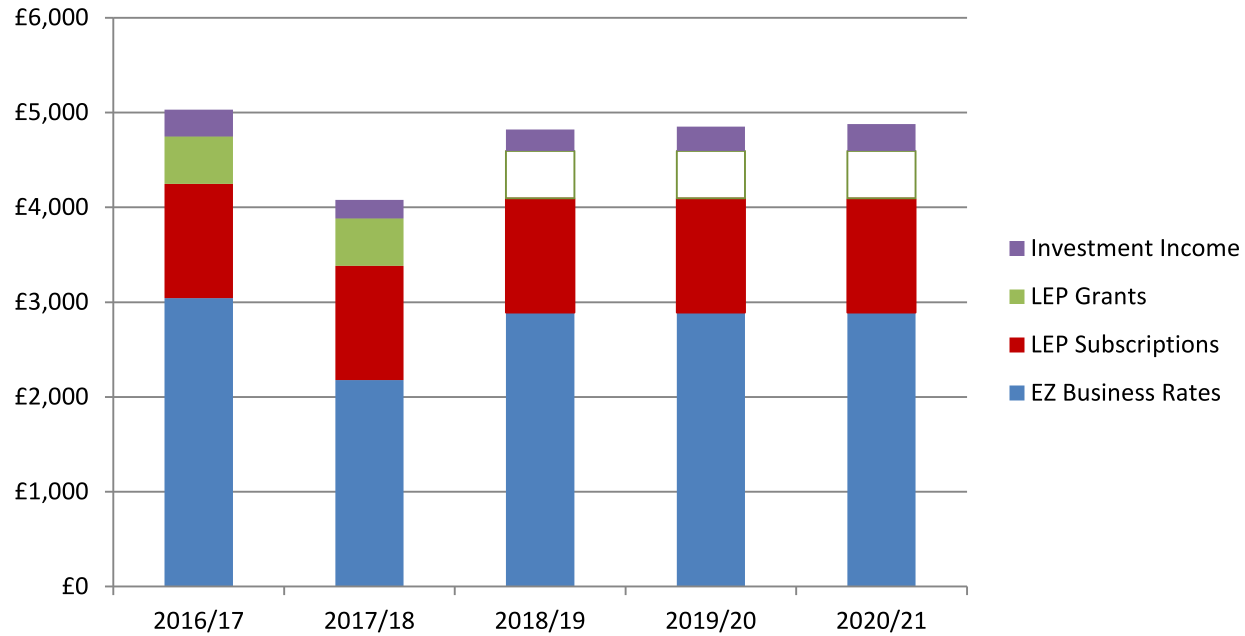
Income

- Significant hit on 17/18 rates gives a one-year problem, before rates expected to recover
- However, LEP grants not committed beyond next financial year, should they be withdrawn we will have a significant problem



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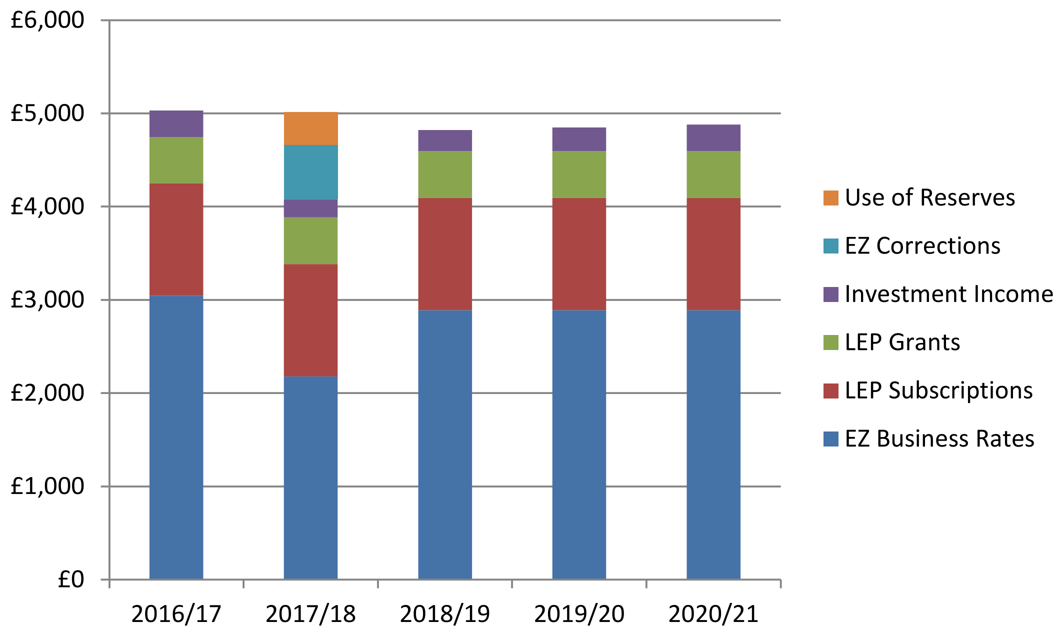
Income

- To sustain budget at 16/17 levels into 17/18:
  - Release unexpected EZ windfall (£585k)
  - Release 16/17 forecast underspend (c. £350k)
- Key point: one-offs and new income needed to retain resource at current levels
  - Resource will fall below current levels unless new income streams are identified



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Expenditure

- Aspirations are pared back to the available resource
- **Magic number c. £5m net**
  - Net after recharges into programmes and capitalised costs
- Short-term planning horizons mean cost mixes remain difficult to balance
- Tensions between the need to recruit to provide capacity whilst also maintaining adequate development resource and discretionary resource to manage significant one-off costs
- Key changes on prior year:
  - Significant one-off costs budgeted for:
    - Devolution consultation and challenge
    - Horasis investment conference
- Resource only allocated to key priorities in consideration of future year pressures

Expenditure - Net

- Modelled on 72 officers plus staffing contingency
  - Costs of staff down due to recruitment strategies
  - Recruits that can be charged into programmes favoured over those that will bring a cost pressure
- Cost pressures in some areas, particularly back office support to reflect up-tick in overall officer numbers and impending activity
- Development and marketing budgets currently fully subscribed
  - £550k set aside for devolution consultation and challenge
  - £250k for Horasis conference
- Available resource c. £150k, allocated to development budget to support in-year opportunities
  - Resource will only be allocated to priority activity in consideration of anticipated future year pressures

	2016/17		**2017/18**		**Variance**
	£'000		**£'000**		**£'000**
Staffing	£2,634	52%	£2,308	46%	£326
SEP Development	£988	20%	£1,150	23%	-£162
Marketing & Communications	£645	13%	£645	13%	£0
Business Support	£280	6%	£455	9%	-£175
Supplies and Services	£346	7%	£288	6%	£58
Accommodation	£100	2%	£103	2%	-£3
Travel	£59	1%	£65	1%	-£6
	£5,052		**£5,014**		**£38**

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Sustainability: Core Activity

- Available resource for core activity falls as wage and price inflation exceeds forecast growth in income

Budgets	2016/17	2017/18	2018/19	2019/20	2020/21
	Base	Forecast	Forecast	Forecast	Forecast
	£'000	£'000	£'000	£'000	£'000
Resource	£5,032	£5,014	£4,820	£4,850	£4,880
Net Costs	£5,032	£5,014	£5,202	£5,300	£5,385
Net	**£0**	**£0**	**-£382**	**-£450**	**-£505**

- To achieve budget sustainability the SCR will need to:
  - Pare back discretionary budgets; and/or
  - Grow its income streams

Budget reductions will inevitably:
  - Fall on non-staffing development and marketing budgets
  - Restrict future recruitment
  - Limit the SCR's ability to take on new activity
- Work is underway to develop means of using LGF resource to return sustainable income streams that could mitigate this pressure
- Future EZ business rate growth from Maclaren will also assist when it comes on-line

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Revenue Programme Activity

- Potentially significant growth due to
  - Employment Support Pilot
  - Health Led Employment Trial
- Employment programmes are not committed to at this stage, and subject to approval both internally and externally
  - Adopting these programmes will change the shape and character of the budget
  - Significant financial and reputational risk
- Work underway on a potential Adult Education programme that could see significant cash flows from 2018/19 (£23m)
- Business growth programmes continue to be resourced from the LGF reserve
  - This is not sustainable in the longer-term
- One Public Estate programme continues to be funded by grant

		Resourced by:	
Revenue Programme Activity	**Expenditure**	**Grant**	**Reserves**
	£'000	**£'000**	**£'000**
Business Growth	£1,346	£410	£936
Skills & Employment	£10,097	£10,097	£0
Other	£186	£186	£0
	£11,629	**£10,693**	**£936**

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Sustainability: Programme Activity

- Business Growth activity is principally funded from the LGF revenue reserve.
- Activity closes in 2020/21, but AFCOE sees a significant reduction in resource before this point
- A viable business model is required for both functions if the activity is to be retained into the future
  - Work required in 2017/18 to develop sustainable propositions

Business Growth Revenue Programme	2017/18	2018/19	2019/20	2020/21	2021/22
	£'000	£'000	£'000	£'000	£'000
Growth Hub	£680	£580	£500	£300	£0
Access to Finance team	£352	£42	£42	£0	£0
Launchpad	£130	£130	£0	£0	£0
RISE	£50	£50	£0	£0	£0
Hub Enhancement	£134	£134	£0	£0	£0
Total Spend	**£1,346**	**£936**	**£542**	**£300**	**£0**

Residual resource has been held within the LGF reserve to allow for a managed close of the current activity:

LGF Revenue Reserve	2017/18	2018/19	2019/20	2020/21	2021/22
	£'000	£'000	£'000	£'000	£'000
Forecast balance b/f	£3,131	£2,195	£1,259	£717	£417
Draws	-£936	-£936	-£542	-£300	£0
Forecast balance c/d	£2,195	£1,259	£717	£417	£417

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Thank you for listening and any questions?

22nd March 2017

CA/LEP Revenue Budget & Medium-Term Financial Strategy

Purpose of Report

This paper proposes a revenue budget for financial year 2017/18, and forecasts for future years. The budget and programmes presented in this paper facilitate the work of the SCR Executive in delivering the Strategic Economic Plan.

This budget has been prepared on the basis that devolution gainshare monies do not flow.

Thematic Priority

All

Freedom of Information and Schedule 12A of the Local Government Act 1972

The paper will be available under the Combined Authority Publication Scheme.

Recommendations

It is recommended that Leaders:

- approve the proposed revenue budget for 2017/18
- note that subscriptions payable by partner authorities will be frozen on 2016/17 levels
- note that there are significant sustainability issues with the CA/LEP revenue budget

1. Executive Summary

1.1 The revenue programmes and budgets discussed in this paper have been prepared on the basis that devolution monies will not flow. In 2016/17 a revenue budget was prepared on a one-year basis in the anticipation that gainshare funding would be received at some point in the year, which would trigger a revised budget.

1.2 It is not now anticipated that the region will receive gainshare in the near-term as uncertainties persist. Accordingly, a medium-term budget has been be prepared that allows the Authority to take a longer-term view of existing resource. Activity plans have been scaled back to meet resource, whilst proposed programme growth will be considered in the context of the capacity of the existing staffing structure.

1.3 Revenue programmes have been developed on the basis of known commitments from government for funding discreet programmes. At this stage, negotiations are underway with government for a number of material strands of activity that are linked to the devolution agenda.

1.4 Of note in the preparation of these budgets and programmes is:

1. Material future year uncertainty around our income streams, in particular retained business rates and capacity grants awarded by government to LEP areas;
2. Insufficient resource to fully recruit to the new SCR Executive structure now that gainshare resource is unavailable;
3. The anticipated need to fund further rounds of devolution consultation, and allocate resource to cover another legal challenge;
4. The need to consider the sustainability of our general budgets and business growth activity that is currently resourced from the finite LGF revenue reserve; and,
5. The potential significant growth in revenue programmes to be operated in the skills and employment work streams which will test the Authority's ability to adequately control and resource the activity within existing capacity

1.5 The Authority will be confronted with a number of challenges in the coming years as it attempts to manage a number of financial difficulties from a position of relative weakness.

1.6 Revenue income streams from government are committed on a year-by-year basis, whilst retained business rates due to the region from the Enterprise Zone remain stubbornly difficult for partners to accurately forecast. This makes medium-term planning difficult, and prejudices the Authority's ability to resource the SCR Executive staffing structure with confidence.

1.7 The region is also exposed to unpredictable costs as the issues around the judicial review and devolution consultation have shown. Provision has been taken within the Authority's budgets to manage these risks, restricting the amount of resource available for other priorities.

1.8 These issues will be exacerbated by the level of risk the region could be exposed to if it is to proceed with plans to take on major new strands of activity around adult education and work and health budgets from government. Balance sheet strength and staffing capacity to take on significant complex new spheres of activity without more financial and human resource will be a key consideration moving forward.

1.9 Set against this, the Authority continues to operate with a relatively low level of reserves to help guard against financial shock. Anticipated outturn underspend from this financial year will be taken to reserves to bolster our financial resilience, whilst it is proposed that some be released to ease income pressures in 2017/18.

1.10 Without gainshare the Authority must seriously consider its funding mix, the call upon partners for resource, and the overriding need to identify sustainable funding streams to allow it to operate with confidence.

1.11 This is a particular concern with respect to key business growth programmes that are currently funded from the LGF revenue reserve. Once this reserve is exhausted, the activity will become unsustainable unless further resource is identified.

1.12 This paper proposes a £5m revenue core budget to be resourced from grants, contributions, retained business rates, and a significant one-off contribution from reserves:

	2017/18
Core Budget	**£'000**
Core Operational Net Expenditure	£5,014
Resourced by:	
Income	£4,079
Use of Reserves	£935
	£5,014

1.13 The paper further proposes revenue programme budgets of:

		Resourced by:	
Revenue Programme Activity	**Expenditure**	**Grant**	**Reserves**
	£'000	**£'000**	**£'000**
Business Growth	£1,346	£410	£936
Skills & Employment	£10,097	£10,097	£0
Other	£186	£186	£0
	£11,629	**£10,693**	**£936**

2. Background

2.1 The resource available to the region to deliver upon its SEP comes in the form of capital and revenue funding.

2.2 The capital programme and revenue budgets set out how that resource will be used in both the forthcoming financial year, but also future years.

2.3 The CA/LEP revenue budgets and capital programme are still relatively immature, reflecting that the Authority is still very much a 'start-up'.

2.4 Activity is growing rapidly, and cost mixes have changed. The SCR Executive has recently undergone a major restructuring exercise that would see staffing numbers grow from c. 30 posts to 97 if fully staffed.

2.5 The capital programme has also grown rapidly, from £0 in 2014/15 to £97m in 2016/17.

2.6 Managing this growth in the face of uncertain income streams is difficult.

2.7 The Authority has a significant capital programme, but limited revenue resource for core functions. This means that the Authority is acting with a relative imbalance in its funding. Revenue resource would allow us to resource teams to ensure that we deploy our capital resource in an efficient and effective manner. Without that revenue resource the Authority continues to operate with under-staffed teams, placing strain on both officers and process.

2.8 This remainder of the report will be divided into the following sections:

1. Forecast revenue reserves;
2. Forecast revenue budgets for the forthcoming years; and
3. Forecast revenue programmes for the forthcoming years.

2.9 The paper will seek to highlight the key financial challenges facing the authority over this period.

3. CA/LEP Revenue Reserves

3.1 The starting point for the CA/LEP revenue budget is to consider the forecast outturn position as at period 11, and the associated impact on the reserves position.

3.2 This shows that the region expects to return a surplus on its core non-programme activity of c. £1.2m.

3.3 This material underspend has arisen for three principal reasons:

1. On-going staffing underspends that have accrued whilst the SCR Executive restructured its establishment structure (net £632k);
2. A material correction on retained business rates due to the region from the Enterprise Zone recognised in financial year 2015/16 (£585k); and,
3. A material improvement on interest income accrued from having cash in interest bearing accounts for much longer than anticipated due to the capital programme slippage (£250k)

3.4 The second issue is an on-going problem that highlights the difficulty partners have in accurately forecasting what rates will be due to the Authority in any one year, let alone future years. The correction recognises that forecasts for income due to the Authority were much lower than actually accrued.

3.5 These underspends mask the costs of the devolution consultation judicial review (c. £250k).

3.6 Accordingly, the Authority expects to go into financial year 2017/18 with general fund reserves of:

CA/LEP Reserves	Status	2016/17	Draw	Contribution	2017/18
		£'000	£'000	£'000	£'000
General Contingency	Available	£646	£0	£1,251	£1,897
LGF Business Growth	Earmarked	£3,869	-£738	£0	£3,131
		£4,515	**-£1,064**	**£1,251**	**£5,028**

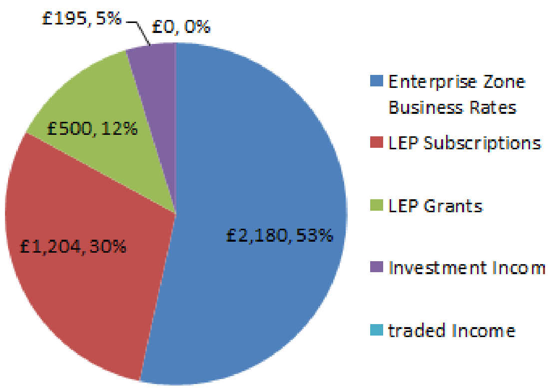
3.6 The LGF business growth reserve is earmarked under agreement with government for business growth activity including the Growth Hub and Access to Finance teams.

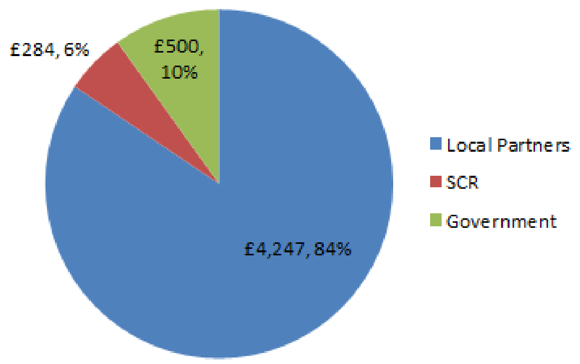
3.7 General contingency reserves form our starting point for dealing with a number of significant pressures that will arise in the coming year.

4. CA/LEP Revenue Budget Proposals

Income

4.1 Income for the CA/LEP budget comes from a variety of sources. In 2016/17 it was made up from the following funding streams and sources:





4.2 <u>Pressures on Income</u>

In 2016/17 the CA/LEP budget forecast to have general income streams of £5,052k. This was revised upwards by £585k at quarter 3 to reflect a correction to Enterprise Zone retained rates.

4.3 The Authority's income forecasts for 2017/18 are materially lower than this at £4,079k, representing an almost £1m reduction:

			2016/17	2017/18	Variance
			Budget	Forecast	
Forecasts	**Funder**	**Status**	**£'000**	**£'000**	**£'000**
Enterprise Zone Business Rates	Local Partners	Forecast	£2,724	£2,890	-£167
Adjustment for Prior Year Enterprise Zone Business Rates	Local Partners	Forecast	£319	-£711	£1,030
Total Enterprise Zone Business Rate Income	**Local Partners**	**Forecast**	**£3,043**	**£2,180**	**£863**
Local Authority Contributions	Local Partners	Committed	£1,204	£1,204	£0
LEP Grants	Government	Committed	£500	£500	£0
Investment Income	SCR	Forecast	£284	£195	£89
Traded Income	SYITA Properties	Committed	£20	£0	£20
			£5,051	**£4,079**	**£972**

4.4 Again, the considerable variance is principally due to a forecast correction on the Enterprise Zone rates due to the region in this financial year. This has arisen because of delays in build completion to a number of significant units opening at Markham Vale, the rates for which had been budgeted in financial year 2016/17.

4.5 Forward forecasting by Chesterfield colleagues indicates that they expect business rates accrued at Markham Vale in 2016/17 to be around £724k below budget assumptions. Final certification of these results will come in the autumn of the next financial year, but means that it is prudent to recognise this write down in income at budget setting for financial year 2017/18.

4.6 It has been previously recognised that the business rates generated from the Enterprise Zone are unsuitable for resourcing sticky costs such as salaries. Inherently, growth on the Enterprise Zone is difficult to forecast, since there are many variables which are outside of the control of billing authorities. In recent years there have been material corrections to budgeted numbers to recognise both shortfalls in income and growth:

	2015/16	2016/17	2017/18
Total	**£'000**	**£'000**	**£'000**
Base Forecasts	£1,208	£2,724	£2,890
Budgeted Adjustments	£0	£319	-£711
Unbudgeted Adjustments	-£15	£585	£0
	£1,193	**£3,628**	**£2,180**

4.7 At the time of writing the Authority's Chief Financial Officer has recommended that the Authority take the unbudgeted surplus generated this year (16/17) immediately to its reserves to be offset against the forecast write down on rates for the following year.

4.8 This will have the benefit of smoothing the spike in income this year and the loss of income in the following year:

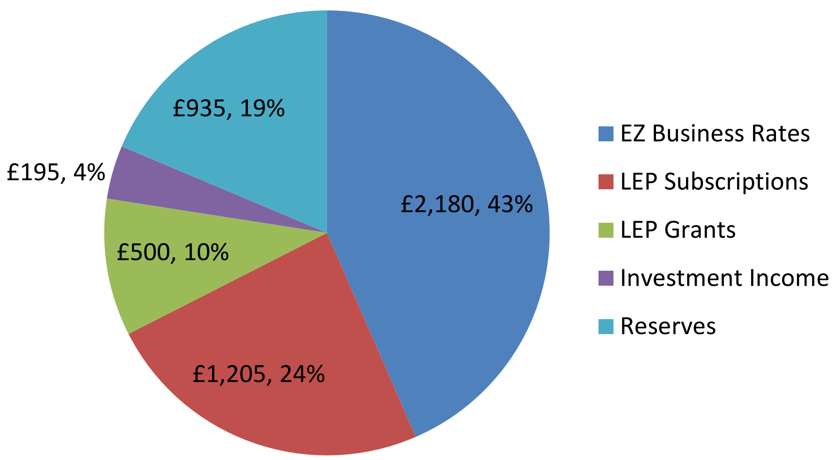
	2014/15	2015/16	2016/17	2017/18	2018/19
EZ Rates	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Forecast Budget	£581	£1,208	£2,724	£2,890	£2,890
Prior Period Adjustments	£0	£0	£319	-£711	£0
Reserve Contributions	£0	£0	£0	£585	£0
Total EZ Resource	**£581**	**£1,208**	**£3,043**	**£2,764**	**£2,890**

4.9 However, despite releasing that reserve the Authority will still have considerably less resource at its disposal than in 2016/17 without further mitigation. To further mitigate the loss of income from the EZ and other sources, it is proposed that a further £350k of forecast revenue underspend from 2016/17 be released to support 2017/18 income pressures:

	2016/17		2017/18		
	Base Budget		**Base Budget**		**Variance**
Forecasts	**£'000**	**%**	**£'000**	**%**	**£'000**
Enterprise Zone Business Rates	£3,043	60%	£2,180	53%	£863
Local Authority Contributions	£1,205	24%	£1,204	30%	£0
LEP Grants	£500	10%	£500	12%	£0
Investment Income	£284	6%	£195	5%	£89
Traded Income	£20	0%	£0	0%	£20
	£5,032		**£4,079**		**£953**
Release of Reserves:					
EZ surplus	£0		£585		£585
General surplus	£0		£350		£350
Total Resource Available	**£5,032**		**£5,014**		**£18**

4.10 That the Authority is able to do this is largely fortuitous. Had the Authority had to write down 2017/18 income by over £700k without recourse to the unexpected surpluses, the Authority would have had to reduce operating budgets considerably or expend the entirety of its general revenue reserve.

4.11 Settling on this income mix highlights that the Authority is heavily reliant on volatile income streams and one-off interventions from reserves:



4.12 Of this income, only £1,205k from local authority LEP subscriptions – or 24% of the budget – is in any way committed from one year to the next. All other income sources are subject to volatility, whether it be through government withdrawing grants, reserves not being available, or fluctuations on the EZ sites as businesses come in or leave the region.

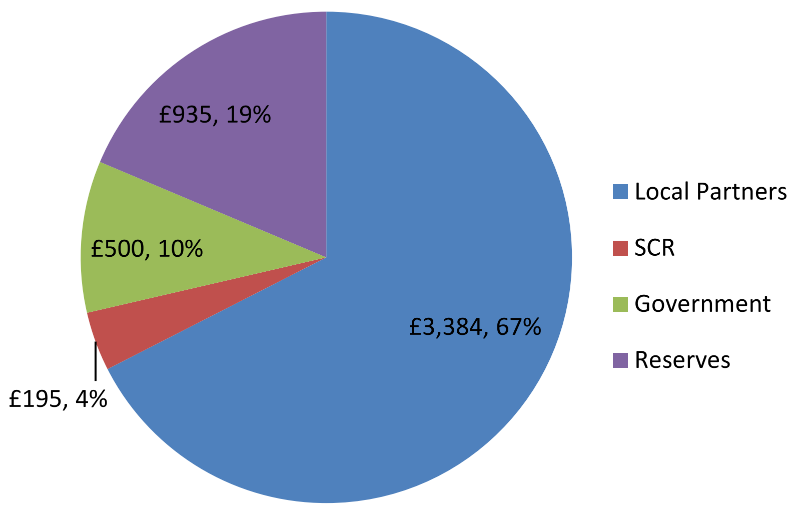
4.13 This uncertainty makes future year planning problematic. The following table shows future year forecasts. At this stage, there is material uncertainty on whether government will continue to pay LEP capacity grants beyond the forthcoming year:

	2016/17	**2017/18**	**2018/19**	**2019/20**	**2020/21**
Income Stream	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
EZ Business Rates	£3,043	£2,180	£2,890	£2,890	£2,890
Local Authority LEP Subscriptions	£1,205	£1,205	£1,205	£1,205	£1,205
LEP Grants	£500	£500	*£500*	*£500*	*£500*
Investment Income	£284	£195	*£225*	*£255*	*£285*
Reserves	£0	£935	*£0*	*£0*	*£0*
	£5,032	**£5,015**	**£4,820**	**£4,850**	**£4,880**

4.14 The table highlights that if government withdraw LEP support, the Authority will lose c. 10% of its income necessitating reductions in discretionary operational budgets or the identification of new funding streams.

4.15 <u>Partner Contributions</u>

Currently, most funding comes from local partners. This is principally through the retained business rates, but also through subscriptions. Subscriptions consist of the 'base' LEP subscriptions of £204k, supplemented by £1m for the costs of the strategic transport hub which was migrated from SYPTE to the SCR Executive.

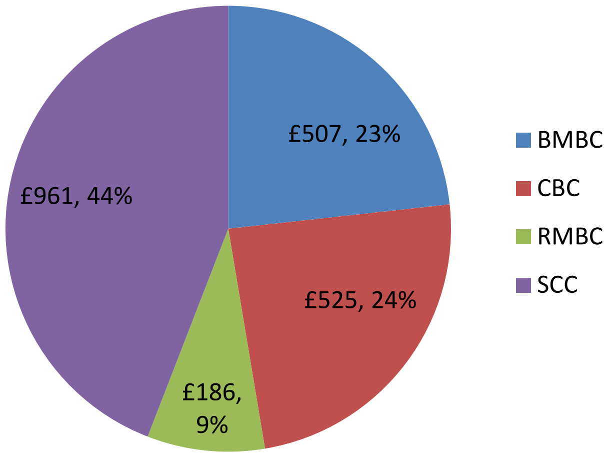


4.16 It is proposed that subscriptions for the coming year will be allocated as follows:

Partner	2017/18 Base £'000	2017/18 Transport £'000	2017/18 Total £'000	2016/17 Total £'000	Variance £'000
Barnsley	£32	£174	£206	206	£0
Bassetlaw	£4	£0	£4	4	£0
Bolsover	£4	£0	£4	4	£0
Chesterfield	£4	£0	£4	4	£0
Derbyshire Dales	£4	£0	£4	4	£0
Doncaster	£41	£222	£263	264	-£1
North East Derbyshire	£4	£0	£4	4	£0
Rotherham	£36	£190	£226	226	£0
Sheffield	£76	£415	£491	489	£2
	£205	**£1,000**	**£1,205**	**£1,205**	**£0**

4.17 Base subscriptions are charged based upon a mechanism agreed in 2013 which has not been revisited since, whilst transport hub contributions are allocated based upon population size at the South Yorkshire level, per the agreement made as part of last year's budget setting process. Variances to 2016/17 represent growth in Sheffield's population compared to the other South Yorkshire districts.

4.18 Enterprise Zone retained rates are forecast to come from the following partners in 2017/18:



4.19 Chesterfield have a higher underlying contribution of £1.25m, but this is affected for the forthcoming year by the write down to 2016/17 forecasts.

4.20 Recharged Income

On top of its general resource the Authority will also look to recharge costs into grant programmes where it is appropriate to do so. This recognises that the costs incurred in delivering programmes should be apportioned to that activity such that there is full cost transparency.

4.21 For the forthcoming year, what we can charge depends largely on:

- What programmes are run;
- What the terms and conditions of grants are; and
- What staffing structure the CA operates.

4.22 Under these budget proposals it is anticipated that the region could recharge costs as follows:

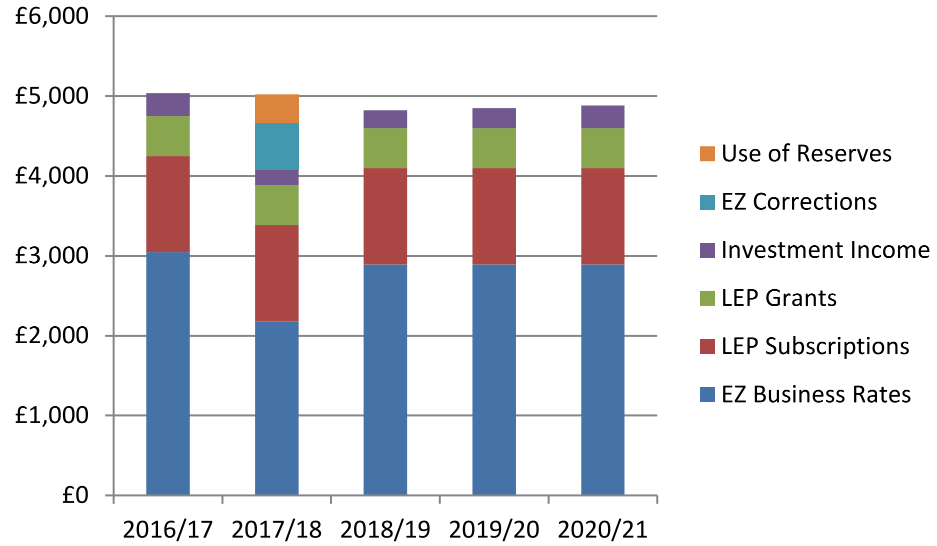
	2017/18
Resource	**£'000**
Gross Income	£5,015
Recharges:	
Revenue programmes	£770
Capitalisations	£1,131
Total Recharges	£1,901
Total Resource	**£6,915**

4.23 Accordingly, the region has gross resource for around £6.9m of activity in 2017/18 (£6.5m 2016/17). This increases the Authority's overall spending power for the year.

4.24 Income Sustainability

The previous pages highlight that resource will be propped up in 2017/18 by reserves (general 2016/17 surplus and EZ business rate corrections).

4.25 In future years, it is anticipated that retained business rates will largely recover to offer a more stable baseline whilst other income streams are also forecast to remain static:



4.26 However, the graphic indicates that future years' income streams are likely to be lower than those enjoyed in 2016/17 and 2017/18.

4.27 This will represent a problem, as the Authority needs income to grow at least in line with cost inflation to ensure that it retains as much spending power as it currently has.

4.28 The region has some cause for optimism in that there is likely to be growth on the EZ due to Mclaren coming to the AMRC EZ site, and potentially also Boeing. The rates paid by these organisations will accrue to the region.

4.29 To ensure income security, it is crucial that the Authority grows its controllable revenue streams to ensure that is not too dependent on income sources that may be withdrawn (such as LEP grants) or that are hard to predict (such as retained business rates).

4.30 As the EZ matures, it is hoped that rates payable will stabilise. Growth will inherently be difficult to predict.

4.31 <u>Expenditure</u>

The Authority's expenditure budgets are largely made up of staffing costs.

4.32 Gross staffing costs made up around 52% of the revenue budget in 2016/17, though the budget for staffing in the year is around £1.3m underspent before the costs of agency staff and consultants.

4.33 This significant underspend has accrued as a result of the SCR Executive's restructure which has taken most of the year to conclude. Whilst this restructure was underway, posts were held vacant and departing officers were not back filled. This placed considerable strain on officers and systems.

4.34 The SCR Executive's restructure has now concluded. The new structure was designed to reflect an operating environment in which gainshare monies would flow, and the Authority would have additional burdens to manage. The structure anticipated 97 officers.

4.35 The cost of this new structure would stand at £4.9m p/a before recharges, and net £3.2m after deductions for rechargeable activity.

4.36 This would represent a material increase on the 2016/17 budget for staffing, with an increase of 35 officers:

	2016/17	**2017/18**	**Variance**
Item	**£'000**	**£'000**	**£'000**
Gross Staffing	£3,285	£4,944	-£1,659
Recharges	£651	£1,774	£1,123
Net Staffing	**£2,634**	**£3,170**	**-£536**
FTEs	**62**	**97**	**-35**

4.37 Without the associated increase in resource that would have flowed from gainshare, this level of staffing cost would not be sustainable without significantly reducing the other budgets that make up the balancing 48% of the authority's net revenue budget in 2016/17.

4.38 These include budgets for marketing and communications, SEP development, supplies and services, and business support functions provided by partners:

2016/17 Budget by Cost Type	**Revised Budget**	
Net Revenue Expenditure	**£'000**	**%**
Staff	£2,634	52%
SEP Development	£988	20%
Supplies & Services	£346	7%
Business Support	£280	6%
Transport	£59	1%
Premises	£100	2%
Marketing & Communications	£645	13%
	£5,052	

4.38 Recognising that a devolution proof structure is not affordable without devolution monies, finance officers have worked with SCR leadership to conduct a resource rationing exercise that helps determine what costs would be affordable from the more limited resource available to the Authority.

4.39 This exercised has produced a prioritised structure, with effective ranking of posts into three generic pools:

1. Committed posts;
2. Business critical posts; and,
3. Activity/resource contingent posts

4.40 This ranking allows us to determine which posts we are currently funding and will continue to do so; those that are critical for the effective running of the Authority; and those that would be recruited to if activity and resource flowed at a later date. Business critical posts reflect those that have been largely filled by temporary resource whilst a recruitment freeze was maintained.

4.41 The aim of this exercise was to fill as many of pools 1 and 2 as possible, whilst also taking account of the associated overhead costs for officers, and the incremental increase in business support costs that would come from more officers and more activity.

4.42 This exercise has resulted in a draft staffing structure based on 72 officers. Ten more than in the 2016/17 budget, but 25 (and 26%) short of the full structure. This structure resources most pool 1 and 2 posts.

4.43 The following table shows the forecast net costs (after recharges into programmes) of the structure:

	FTE	Gross	Recharges	Net Cost
		£'000	£'000	£'000
Business Support and Investment	3	£175	£27	£148
Corporate Services	8	£312	£57	£255
External Capital Programme	6	£318	£318	£0
Growth Hub	11	£395	£395	£0
Growth Hub 2	1	£73	£73	£0
Housing, Investment & Planning	3	£176	£84	£92
Investment	5	£271	£0	£271
Operational Contracts	6	£291	£156	£135
Programme Management Office	5	£254	£254	£0
Policy	5	£283	£1	£282
Programme Assurance	3	£180	£136	£44
Skills, Employment & Education	4	£217	£16	£201
SLT	3	£387	£137	£250
Strategy and Corporate Affairs	6	£313	£0	£313
Transport	3	£171	£5	£166
	72	**£3,818**	**£1,659**	**£2,158**
Contingency				£150
Total Staffing				**£2,308**

4.44 Contingency is held to deal with potential issues that may arise as a result of protracted recruitment periods; recruitment fees; and the uncertainty on final salary costs for officers to be recruited.

4.45 Despite the increase in officers this cost compares favourably against the current budget of £2.6m, and recognises – in part – the work done to properly apportion costs to programmes of activity.

4.46 The following table shows how the cost composition of the net budget (after recharges and capitalisations) fares against the prior year these proposals.

	2016/17		2017/18		Variance
	£'000		£'000		£'000
Staffing	£2,634	52%	£2,308	46%	£326
SEP Development	£988	20%	£1,150	23%	-£162
Marketing & Communications	£645	13%	£645	13%	£0
Business Support	£280	6%	£455	9%	-£175
Supplies and Services	£346	7%	£288	6%	£58
Accommodation	£100	2%	£103	2%	-£3
Travel	£59	1%	£65	1%	-£6
	£5,052		**£5,014**		**£38**

4.47 The increase in costs associated with business support reflect the request from the SCR Executive in consultation with the statutory officers for increased professional support as programmes develop, with the cost increase equating to one additional legal, finance, and procurement officer.

4.48 Total business support costs are forecast as follows:

	Cost	Recharge	Net Cost
	£'000	£'000	£'000
Finance	£200	£26	£174
Legal, Governance, HR	£210	£4	£206
Procurement	£50	£0	£50
Internal Audit	£25	£0	£25
	£485	**£30**	**£455**

4.49 It is anticipated that if the region is successful in its bids into government for funding towards work and health programme activity, that some more of these costs can be recharged against new funding lines to reflect the additional burden that will fall on these teams.

4.50 Much work has been undertaken during the year to identify cost savings in supplies and services, and drive down accommodation costs by sharing services with SYPTE. This has resulted in a c. £58k decrease on the costs to the Authority of supplier and services.

4.51 SEP development budgets are allocated on a bidding basis to ensure that there is focus and corporate control on the use of advisors. This budget resourced 33 individual commissions in 2016/17 including the review into governance, the SEP refresh, and other key activities.

4.52 In the new year, known pressures around the need for a transport strategy refresh, and a potential further round of devolution consultation and associated legal costs mean that it is prudent to retain a significant resource for this activity. As c. £550k will be set-aside to manage the devolution process with confidence, it is proposed to top-up this budget line with additional resource to allow the Authority to proceed with confidence.

4.53 In the forthcoming year, it is anticipated that the development budget will, amongst other things, further resource:

- The SEP refresh;
- The transport strategy refresh;
- The gainshare national evaluation costs;
- An asset management review; and,
- Work in support of the proposed employment programmes.

4.55 Marketing and communication budgets are similarly held corporately and distributed on a bidding basis. This budget is expected to resource the Horasis conference in 2017/18 (c. £250k) and continue to support LEP priority areas around communication.

4.56 The following table shows the inflationary impact of the expenditure items over time. Staffing costs have been inflated to reflect movement through the BMBC grading structure with pay awards at 1%, whilst other costs are also inflated by 2% for Bank of England target inflation:

	2017/18	2018/19	2019/20	2020/21
Net Budget Costs	**£'000**	**£'000**	**£'000**	**£'000**
Staffing	£2,308	£2,442	£2,485	£2,513
SEP Development	£1,150	£1,173	£1,196	£1,220
Marketing & Communications	£645	£658	£671	£684
Business Support	£455	£464	£473	£483
Supplies and Services	£288	£293	£299	£305
Accommodation	£103	£105	£108	£110
Travel	£65	£66	£68	£69
	£5,014	**£5,202**	**£5,300**	**£5,385**

4.57 The table highlights the significant impact of inflation on costs - which adds £371k onto the cost of activity by 2021 – along with the impact of reductions on recharges for officer time as time-limited grant programmes end.

4.58 Core Revenue Budget Sustainability

Based on these estimations, unless budgets were adjusted to meet resource the Authority would run into material deficits by 2018/19, which would then quickly escalate:

Budgets	2016/17	2017/18	2018/19	2019/20	2020/21
	Base	**Forecast**	**Forecast**	**Forecast**	**Forecast**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Resource	£5,032	£5,014	£4,820	£4,850	£4,880
Net Costs	£5,032	£5,014	£5,202	£5,300	£5,385
Net	**£0**	**£0**	**-£382**	**-£450**	**-£505**

4.59 The Authority could commit additional reserves to meeting some of these deficits, but that would not be a sustainable solution.

4.60 Instead, the Authority would be required to either pare discretionary activity back to resource or grow its other income sources.

4.61 Although the Authority does expect some growth on the EZ sites as a result of landing Mclaren in recent weeks, it is likely that the Authority will have to reduce its development budgets to balance.

4.62 This will limit the Authority's ability to undertake studies and research which will add value to the SEP, and conduct LEP priority activity around marketing and communication in support of inward investment.

4.63 To meet its budget targets - and reduce reliance on government and partners - the Authority requires a re-think on how it can deploy its wider resource to generate sustainable income streams. This could come in a number of ways from strategic acquisitions that generate income to interest bearing investment loans.

5. Revenue Programme Activity

5.1 Revenue programme activity consists of the time-limited pieces of work that are funded discreetly from grant.

5.2 These grant work streams principally fall around the business growth and skills work streams.

5.3 Over the coming years this activity is forecast to increase dramatically in the skills and employment area as devolution of powers and funding could potentially progress three new work streams. It is worthy of note, however, that the two principal programmes were part of the devolution deal, with the final programme was linked to one of the devolution programmes.

5.4 <u>Business Growth</u>

In 2015, the region agreed with government to 'swap' £4m of capital resource for revenue grant. Government agreed to the request on the proviso that the grant would be spent on business growth activity.

5.5 This grant was taken to the Authority's reserves and is now released on an annual basis to meet the costs of the Growth Hub and Access to Finance teams, along with individual projects that support the business growth aspirations.

5.6 This activity has also been supported for the past two years by direct government grant funding for the Growth Hub, which has allowed the region to extend the period over which the Hub would operate by a further year. The region will receive a further tranche of £410k funding for the Hub in 2017/18.

Business Growth Revenue Programme	2017/18	2018/19	2019/20	2020/21	2021/22
	£'000	£'000	£'000	£'000	£'000
Growth Hub	£680	£580	£500	£300	£0
Access to Finance team	£352	£42	£42	£0	£0
Launchpad	£130	£130	£0	£0	£0
RISE	£50	£50	£0	£0	£0
Hub Enhancement	£134	£134	£0	£0	£0
Total Spend	**£1,346**	**£936**	**£542**	**£300**	**£0**

5.7 The table usefully highlight that activity cease under current forecasts by 2020, presenting the region with a cliff-edge in provision.

The activity's funding principally comes from the LGF reserve:

Business Growth Revenue Programme	2017/18	2018/19	2019/20	2020/21	2021/22
Funding	£'000	£'000	£'000	£'000	£'000
Growth Hub grant	£410	£0	£0	£0	£0
LGF Reserve	£936	£936	£542	£300	£0
Total Resource	**£1,346**	**£936**	**£542**	**£300**	**£0**

5.8 The LGF reserve profile is forecast to be in credit over this period principally due to the delay in AFCOE activity in 2015/16:

LGF Revenue Reserve	2017/18	2018/19	2019/20	2020/21	2021/22
	£'000	£'000	£'000	£'000	£'000
Forecast balance b/f	£3,075	£2,139	£1,203	£661	£361
Draws	-£936	-£936	-£542	-£300	£0
Forecast balance c/d	£2,139	£1,203	£661	£361	£361

5.9 This balance could be used to support an extension of AFCOE's activity into the future. AFCOE provide advice to business seeking financial support for growth, but also provide the Business Investment Fund work stream with financial appraisals on businesses seeking grant from the fund.

5.10 Without this provision, the BIF panel of LEP members and SCR officers would be unable to make informed decisions on a businesses' suitability for support. As such, it is likely that the role AFCOE play will need to be replicated even if the delivery model does not remain the same.

5.11 Equally, the region faces a cliff-edge in provision relating to the activity of the Growth Hub. The Hub is staffed with officers on fixed –term contracts, so theoretically the activity could be stopped once funding runs out.

5.12 However, should the region and partners wish to sustain the activity into the future, a new funding source will be required to enable it to continue.

5.13 <u>Skills and Employment</u>

The SCR skills and employment team have been successful over the last few years in attracting government grant for their activity.

5.14 This activity is normally delivered by partner organisations on an agency basis, with the SCR acting as strategic commissioners.

5.15 In 2017/18 it is likely that number of grant funded activities will be under way, whilst there is also ongoing discussion with government around the devolution of significant powers and funding for adult education budgets, an employability pilot, and a working health trial.

Skills & Employment Revenue Programmes	2017/18	2018/19	2019/20	2020/21	2021/22
	£'000	£'000	£'000	£'000	£'000
Skills:					
Apprenticeship Grant for Employers	£657	£0	£0	£0	£0
Skills Bank	£221	£0	£0	£0	£0
Work and Health Programme	£58	£0	£0	£0	£0
Enterprise Advisor Pilot	£63				
Adult Education	£0	*£23,200*	*£23,200*	*£23,200*	*£23,200*
Potential Employment Programmes:					
Employment Support Devolution Pilot	*£3,000*	*£3,000*	*£3,000*	*£0*	£0
Employment Support Devolution Pilot Management & Administration	*£278*	*£248*	*£251*	*£109*	*£110*
Health Led Employment Support Trial	*£5,500*	*£5,500*	*£0*	*£0*	*£0*
Health Led Employment Support Trial Management & Administration	*£320*	*£285*	*£245*	*£0*	*£0*
	£10,097	**£32,233**	**£26,695**	**£23,309**	**£23,310**

5.16 At this stage there is material uncertainty on the three large programmes to commence in 2018. All programmes are still under negotiation with government, at various stages of approval.

5.17 A working group has been set up with the SCR Executive that is considering implementation plans, and the possibility of using European resource to increase the value of the activity. Programme management and administration costs have been built into the draft implementation plans to ensure the work stream can be adequately managed.

5.18 Should these programmes progress the region will need to consider the financial risk around operating such large programmes on both its current capacity and balance sheet strength.

5.19 The larger and more complex the programmes the SCR will enter into, the more it will require stable and adequate reserves to manage the inevitable risk on activity. It is unlikely that the current level of reserves will remain appropriate should these programmes be entered into. Operating complex programmes to this value will also place serious strain on existing capacity, systems, and structures. The Authority will need to seriously consider whether it can adequately resource and control this activity without the gainshare resource that would have resourced the larger SCR structure.

5.20 <u>Reserve Profile</u>

Should the Authority proceed with revenue budgets as detailed in this paper, reserve profiles would change as follows:

CA/LEP Reserves	Status	2017/18	Draw	Contribution	2018/19
		£'000	£'000	£'000	£'000
General Contingency	Available	£1,897	-£935	£0	£962
LGF Business Growth	Earmarked	£2,805	-£936	£0	£1,869
		£4,702	**-£1,871**	**£0**	**£2,831**

5.21 It is not anticipated that there would be further material draws on contingency reserves in future years. The one-off pull in 2017/18 is a mitigation to counter the significant reduction in available income that came from the correction in business rates forecasting.

6. Implications

6.1 Financial

This paper proposes a revenue budget for the Authority in 2017/18, and forecasts for future years.

The paper notes the material uncertainty around income streams which make planning uncertain.

Income is expected to fall by c. £1m in 2017/18 due to anticipated corrections on retained business rates accrued on the EZ. To counter this loss of income, reserves will be drawn upon on a one-off basis.

The paper notes that on a medium-term basis, the current level of expenditure is unsustainable as cost inflation outgrows income. Discretionary budgets will have to be trimmed unless there is growth in income.

The paper further notes the revenue programme activity. This is marked by anticipated growth in employment programmes, but sustainability problems in business growth programmes as finite grant resource is exhausted.

6.2 Legal

None

6.3 Risk Management

The Authority must consider how it manages the sustainability problems within the budget.

Without proper management these issues will deliver unplanned issues that will be detrimental to service delivery.

6.4 Equality, Diversity and Social Inclusion

None

7. Communications

7.1 N/A

8. Appendices/Annexes

8.1 None

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Other sources and references: None