

## Appendix 6

### **Budget and Council Tax 2016/17 – Report of the Chief Financial Officer on the robustness of the estimates and the adequacy of reserves**

#### **1 Introduction**

The Chief Financial Officer is required to make a statement on the adequacy of reserves and the robustness of the budget. This is a statutory duty under section 25 of the 2003 Local Government Act which states the following:

*(1) Where an authority to which section 32 or 43 of the Local Government Finance Act 1992 (billing or major precepting authority) or section 85 of the Greater London Authority Act 1999 (c.29) (Greater London Authority) applies is making calculations in accordance with that section, the chief finance officer of the authority must report to it on the following matters:-*

*(a) The robustness of the estimates made for the purposes of the calculations; and*

*(b) The adequacy of the proposed financial reserves.*

*(2) An authority to which a report under this section is made shall have regard to the report when making decisions about the calculations in connection with which it is made.*

This includes reporting and taking into account:

- The key assumptions in the proposed budget and to give a view on the robustness of those assumptions; and
- The key risk areas in the budget and to assess the adequacy of the Council's reserves when reviewing the potential financial impact of these risk areas on the finances of the Council. This should be accompanied by a Reserves Strategy.

This report has to be considered and approved by Council as part of the budget approval and Council Tax setting process.

This document concentrates on the General Fund 2016/17, the Housing Revenue Account and Capital Programme but, in addition, it also considers key medium term issues faced by the Council.

#### **2 Assurance Statement of the Council's Section 151 Officer (Head of Corporate Finance)**

The following are the summary assurances and recommendations of the Council's Section 151 Officer (the Interim Chief Financial Officer).

In relation to the 2016/17 General Fund Revenue budget I have examined the budget proposals and I believe that, whilst the spending and service delivery proposals are challenging, they are nevertheless achievable (subject to the more significant risks in paragraph 2 below) given the political and management will to implement the changes, good management, and the sound monitoring of performance and budgets. I am satisfied that sufficient management processes exist within the Council to deliver this budget and to identify and deal with any problems which may arise unexpectedly during the year.

The Council's Policy, Finance & Development Committee has received reports setting out the savings proposals and the delivery of those with the greatest risk will be regularly monitored by the Senior Management Team. For 2016/17 the key risks relate to planned savings in the establishment budget. They fall within three categories:

- a) Reductions in the use of agency, contractor and interim staff. SMT will increase the controls over the authorisation of temporary appointments to mitigate this risk;
- b) Savings from the current establishment. The achievement of these savings is considered low risk given that they are based on the current level of vacancies within the staffing budget;
- c) Savings from a further review of establishment across the Council's services. At this stage this review has not started and is therefore considered the highest risk proposal.

These risks are known and work continues to improve this position.

My recommendations are also conditional upon:

- The agreement of a Medium Term Financial Strategy and Plan for 2017/18 to 2019/20 that will require significant reductions in net revenue expenditure to deliver a balanced budget for the financial years 2017/18 and beyond;
- A recognition in the medium term planning approach that the level of reserves and corporate risk assessment need to be regularly reviewed in the light of changing circumstances and that it may not be possible to match the two at any single point in time. The Council needs to show a commitment to maintain reserves at a level which provides adequate cover for most identified risks during the planning period. This approach is pragmatic and shows a clear commitment to prudent contingency planning. It must be noted, however, that the recommended levels of reserves still leave the Council exposed to the very exceptional risks identified in this review and, if those risks crystallise, to reserves being inadequate;
- Committees, Directors and budget holders managing within their cash limits for 2016/17 (and future years covered by the Medium Term Financial Strategy and Plan);

- Taking every opportunity to meet the Reserves Strategy as a first call on windfall underspends or receipts;
- Not considering further calls on reserves other than for those risks that have been identified, those that could not have been reasonably foreseen and that cannot be dealt with through management or policy actions. The exception to this is where the Reserves Strategy (reviewed annually) is met. Even in those circumstances, it is not prudent to finance ongoing spending from one-off reserves. Any excess reserves should be targeted towards one-off 'invest to save', supporting the transition that is required for future service delivery and contributions to fund the Council's capital programme;
- Where there is a draw-down on reserves, which causes the approved Reserves Strategy to be off target, that this is paid back within a maximum of three years; and
- That the Council has arrangements and resources in place to consider value for money in preparation for future years' budgets.

### **3 Reserves Strategy**

In relation to the adequacy of reserves, I recommend the following Reserves Strategy based on an approach to evidence the requisite level of reserves by internal financial risk assessment:

- An absolute minimum level of General Fund reserves of 5% of annual net expenditure that is maintained throughout the period between 2016/17 to 2019/20;
- An optimal level of reserves of between 5% and 10% of annual net expenditure over the period 2016/17 to 2019/20 to cover the absolute minimum level of reserves, in-year risks, cash flow needs and unforeseen circumstances;
- A maximum recommended level of reserves of 10% of annual net expenditure for the period 2016/17 to 2019/20 to provide additional resilience to implement the Medium Term Financial Plan;
- A Reserves Strategy to maintain the recommended optimal level of reserves within the relevant period (2016/17 to 2019/20); and

- In relation to the Housing Revenue Account (HRA) my recommendation is that reserves be maintained at a minimum of £300,000.

The Reserves Strategy will need to be reviewed annually and adjusted in the light of the prevailing circumstances.

The estimated level of unallocated General Fund reserves at 31 March 2016, based on current projections is 15.8% depending on final spending, which remains above the maximum recommended level. The next iteration of the Council's Medium Term Financial Strategy will address this issue further.

These recommendations are made on the basis of:

- The risks identified in the managers' reviews of their budgets;
- The detailed discussions that have taken place at SMT, including the regular review of the high risk proposals;
- My own enquiries during the development of the budget;
- The resilience required to deliver the Medium Term Financial Plan;
- One-off unallocated reserves not being used to fund new ongoing commitments;
- Reserves in 2016/17 and the foreseeable future being used only where planned and if risks materialise and cannot be contained by management or policy actions; and
- That where reserves are drawn down, the level of reserves is restored within a maximum of three years to that required by the Medium Term Financial Strategy.

There are also serious exceptional risks over and above those mentioned which, if they crystallise, could eliminate the Council's reserves and leave its financial standing seriously in question. These include:

- Not realising the efficiencies from transformation and new ways of working;
- Unforeseen impacts arising from the consequences of welfare reform, in particular the roll out of Universal Credit;
- The impact of the localisation of business rates and the consequences of future changes in the total rateable value of businesses located in Oadby & Wigston;
- The impact of changes to New Homes Bonus and other Government grants;
- Unanticipated changes to interest rates;

- Further Government controls on the levels of rent and Council Tax the Council can set;
- Any shortfall against the expected value of assets identified for disposal; and
- The lack of contingency funds to meet demographic and economic pressures, especially at this time of significant change.

In relation to the General Fund and HRA Capital Programme 2016/17 (including commitments from previous years):

- The HRA Capital Programme will need to be contained within total programme costs;
- The General Fund Capital Budget is based on the best information available in terms of project costs. What is less certain, given the history of cost variations, is the phasing of expenditure; and
- The strategic schemes identified in the Capital Programme will be closely monitored in-year.

### **Assurance**

Given all these factors I, as the Council's Section 151 Officer, consider the estimates for 2016/17 to be sufficiently robust but challenging for approval by the Council. I advise the Council that the General Fund Reserves are currently above the optimum level required to ensure financial stability over the medium term and recommend that the Reserves Strategy be maintained in 2016/17 and the medium term.

Martin Hone

Interim Chief Financial Officer

February 2016

## **Supporting Statement**

### *Processes*

Budget estimates are exactly that – estimates of spending and income made at a point in time and which will change as circumstances change. This statement about the robustness of estimates cannot give a 100% guarantee about the budget but gives Members reasonable assurance that the budget has been based on the best information available at the time.

In order to meet the requirement on the robustness of estimates a number of key processes have been put in place, including:

- The issuing of clear guidance to services on preparing budgets;
- The development of Council wide risk assessment;
- The use of budget monitoring to identify risk;
- The Council's S151 Officer providing advice throughout the process of budget preparation and budget monitoring;
- The SMT's review of their budgets, budget sensitivities and regular monitoring of the higher risk proposals;
- A review of budget proposals by SMT throughout the past year;
- A review of budget information by Members, Service Delivery Committee and Policy, Finance & Development Committee throughout the past year; and
- Enquiries made directly by the Section 151 Officer.

Notwithstanding these arrangements, which are designed to test the budget throughout its various stages of development, considerable reliance is placed on SMT and Heads of Service having proper arrangements in place to identify issues, project costs, assess service demands, consider value for money and efficiency, and implement changes in their service plans. This work is supported by appropriately qualified and experienced financial staff.

A summary of the key budget assumptions considered by services in terms of assessing the robustness of their budgets were:

- The treatment of inflation and interest rates;
- The treatment of demand led pressures;
- The treatment of efficiency savings/productivity gains;

- The financial risks inherent in any significant new funding partnerships, major outsourcing deals or major capital developments;
- The availability of other funds to deal with major contingencies;
- The Council's track record in budget and financial management;
- The Council's capacity to manage in-year budget pressures; and
- SMT's ability to manage any pressures that cannot be contained within a service.

#### *Robustness of Estimates – General Fund Revenue Budget*

The 2016/17 budget and service planning process continues the need to link financial resources to corporate priorities and risks. In addition to improving efficiency, there are clearly choices for the Council in this respect:

- To increase financial resources to meet demand and reduce risk; or
- To reduce (where possible) service levels and standards, frequency of service delivery, and eligibility for services.

As part of developing the budget, Members of the administration have considered these options and they are reflected in the proposed budget.

Most notably the Council has had to address major cost increases and pressures as well as corporate priorities including:

- Demographic changes;
- The cost of unsupported borrowing within the capital programme;
- Shortfalls in income;
- Reductions in grant from government; and
- The impact from business rate appeals.

#### *Adequacy of Reserves – General Fund Revenue Budget*

Under the Local Government 2003 Act the Secretary of State has reserve powers to set a minimum level of reserves. The most likely use of this power is where an authority is running down its reserves against the advice of their S151 Officer.

Determining the appropriate level of reserves is not a precise science. It is the Council's safety net for risks, unforeseen events or other circumstances. The reserves must last the lifetime of the Council unless contributions are made from future years' revenue budgets. The minimum level of balances cannot be judged merely against the current risks facing the Council as these can and will change over time.

Determining the appropriate level of reserves is a professional judgement based on local circumstances including the overall budget size, risks, robustness of budgets,

major initiatives being undertaken, budget assumptions, other earmarked reserves and provisions, and the Council's track record in budget management.

The consequences of not keeping a minimum prudent level of reserves can be serious. In the event of a major problem or a series of events, the Council would run a serious risk of a deficit or of being forced to cut spending during the year in a damaging and arbitrary way.

The recommendation on the prudent level of reserves has been based on the robustness of estimate information and the Corporate Risk Register. In addition, the other strategic operational and financial risks taken into account when recommending the minimum level of unallocated General Fund reserves include:

- There is always some degree of uncertainty over whether the full effects of any planned savings and/or service reductions will be achieved. SMT have been requested to be challenging but realistic in their assumptions and that those assumptions, particularly about demand led budgets, will hold true in changing circumstances;
- The Bellwin Scheme Emergency Financial Assistance to Local Authorities provides assistance in the event of an emergency. The Council is able to claim assistance with the cost of dealing with an emergency over and above a threshold set by the Government;
- The risk of major litigation, both current and in the future;
- The risk of losing subsidy arising from outstanding Housing Benefit and Council Tax Benefit Subsidy Claims;
- Unplanned volume increases in major demand led budgets;
- Any event that closes a material business rate payer in Oadby and Wigston and larger than estimated awards to business rate appeals;
- The need to retain a general contingency to provide for some measure of unforeseen circumstances which may arise. This part of the reserves is not provided for directly but indirectly on the assumption that the financial risks identified will not all crystallise within the same financial year; and
- The need to retain reserves for general day-to-day cash flow needs. This is minimal given the level of cash the Council holds at any given time.

#### *Estimated Earmarked General Fund Revenue Reserves*

I have reviewed the Council's earmarked revenue reserves. The amounts held for General Fund purposes are minimal having previously taken the opportunity to rationalise the earmarked reserves to support the transition that the Council is both currently and will be going through over the medium term.

#### *The Capital Budget*



Projects included in the Capital Programme were prepared by Heads of Service and Managers in line with financial regulations and guidance. All projects were agreed by the relevant SMT and Members and are fully funded for their estimated cost.

Projects have been costed at outturn prices with many subject to tender after inclusion in the programme. This may lead to variances in the final costs.

Services are required to work within the given cash envelope so any under or over provision must be found within these limits.

### *Capital Programme Risks*

The risk of the Council being unable to fund variations in the programme is minimal mainly due to phasing of projects. The Council is able to freeze parts of the programme throughout the year to ensure spend is within the agreed financial envelope, although this will have service implications. A further key risk to the capital programme is the ability of the Council to fully deliver it within the agreed timescales.

In relation to the General Fund and HRA Capital Programme 2016/17 (including commitments from previous years):

- The HRA Capital Programme will need to be contained within total programme cost by delaying or stopping specified schemes if necessary;
- The General Fund Capital Budget is based on the best information available in terms of project costs. What is less certain, given the history of underspends, is the phasing of expenditure; and
- The strategic schemes identified in the Capital Programme will be closely monitored in-year.

