Annex 1.2

Budget and Council Tax 2014/15 - Report of the Chief Financial Officer on the Robustness of the Estimates Made for the Purpose of the Budget and Tax Setting Calculations and the Adequacy of the Proposed Financial Reserves.

Budget Proposals

I am satisfied that the process employed for identification, evaluation and inclusion of the items forming the budget proposal package has been properly conducted and has arrived at a set of robust estimates given the limitation placed upon it resulting from the late announcement of the Government Grant Settlement.

In arriving at this opinion I have taken due account of the following matters:

1. Budget Process

a) Budget planning has been undertaken over an appropriate period of time and has allowed full understanding of the issues in an operational and financial context.
b) Every effort has been made to include all Members in the financial planning process through the circulation of reports and associated information. Formal and informal meetings with Members have taken place to discuss budget matters and a Member Workshop was held last year to highlight the budget process.
c) Representatives of those bodies impacted by the savings proposals have been consulted and their views have been taken into account. This in particular has occurred with a Tenants' Panel meeting and discussion regarding the Housing Budget and proposed rent increases.
d) Consideration has been given to the updated corporate plan in formulating the budget proposals. Ongoing reductions in Council funding have meant that the emphasis on resource targeting is now more about where to avoid reductions as opposed to where to invest.
e) The budget formulation process at Officer level has been subject to on-going review which has tested the validity and deliverability of pressures and options so as to ensure that Members have been made aware of all aspects and implications of actions when formulating the budget proposals.

Key Assumptions

In formulating budget proposals it is necessary to make certain key assumptions; these are as follows:

a) Income from business rate retention - the new Government Grant System introduced from 1st April 2013 links Council finances in part to the success of the local businesses. Councillors are likely to gain from the proportion of real business rate growth and lose a proportion of income associated with business rate losses. The budget proposal takes a balanced view on the prospects for growth versus the risk of losses pending the results of the first year's outturn position. The central position should be for a neutral outlook. Work will be undertaken to improve forecasting and to better understand the operation of the system over the following years.

b) In 2013/14, the Council joined a pool arrangement with other Leicestershire authorities for the retention of business rates. During 2013/14 the Business

Rate Pool performance has been monitored and the inherent risk in pooling has increased in the last 12 months. Because of these uncertainties and the high level of risk it was agreed between Leicestershire Authorities that the pool be terminated for 2014/15.

c) Localised Council Tax Support – the Council approved a revised scheme in January 2014 and it is considered that a fair assessment of the likely impact of these changes has been built into the budget in 2014/15. The possibility that these estimates are over or understated is a risk to the budget.

d) Pay and Prices – the proposals include provision for inflation only where there are specific known contractual obligations. An allowance of 1% has been built into the budget for pay.

e) A 2% per annum increase in employer's pension contributions has been provided (as determined by the latest triennial valuation of the Leicestershire Pension Fund in 2013).

f) Demand Changes – the impact of the changes to the welfare and benefits system cannot be assessed before such time as these have been implemented and operational for a while. There is a risk that a consequence of these changes will be an increased demand for housing, advice and support services. The proposals reflect the best assessments of expected changes in demand but there is considerable uncertainty in this respect.

g) Fees and Charges – due account has been taken of the Council's charging policy and provision made for increases in charges where appropriate. Expected volume changes are also included.

h) Council Tax Base and Collection Rate – the assumption of growth in the tax base reflects the historic average of around 0.5%. This is masked by reductions in the tax base to reflect the impact of the Localised Council Tax Support Scheme. The collection rate remains uncertain and performance will be closely monitored over the forthcoming year in order to assess the impact of changes to this Council including discounts and exemptions.

i) Interests and Investments – The outlook for interest rates remains depressed. The best estimate is that they will continue to remain low for two to three years and then increase gradually. An assumption of possible interest rates has been made for the purpose of the budget. The cash flow implications of the Capital Programme have been taken into account in calculating the interest earning available for budget planning.

j) Income Volatility – in some areas of income such as local land charges, building control and planning fees because of the current economic climate it has been difficult to forecast levels. Consequently, it is proposed that that a new Income Profiling Reserve in the sum of £150,000 is set up.

k) Government Grants – outside of the unknown impact of business rate growth or contraction, the allocations of government grants have become confirmed for 2014/15 and 2015/16. This therefore extends up to the next national election in 2015. The government has indicated it is working on a comprehensive spending review which will extend until at least 2017. Other than supposition there are no indicative estimates of the scale of reduction beyond 2016 and so the Council's updated Medium Term Financial Strategy (MTFS) will have to include some realistic assumptions.

l) New Homes Bonus Scheme – the budget reflects the approach to allocations as previously agreed and reported to Council.

m) Revenue Implications of Capital Schemes – revenue implications of those capital investments approved by the Council have been reflected in the budget. The central condition is that the schemes are at least revenue neutral.

Monitoring

The performance against budget for 2013/14 has been monitored throughout the year. The latest outturn estimates (an underspend of £58,446) has been allowed for when estimating the level of resources available for 2014/15 and subsequent years.

The budgetary pressure facing the Council is widely understood and budget holders and managers are working hard towards making savings through efficiency and slimmer structures. As opportunities present themselves, e.g. natural staff turnover, they have been taken and budgetary savings have been realised. These savings are then being reflected in the base budget for future years.

Whilst every years' budget is subject to regular monitoring its importance will remain high during 2014/15 in order to control cost pressures, prevent avoidable overspending and capture under-utilised budgetary provision early.

The Council undertakes regular monitoring and reporting.

Financial Risks in the Budget Proposals

The budget always contains areas of uncertainty and whilst every effort is made to understand, recognise and manage risks adequate financial provisions are held in the event that they cannot be contained. This provision is in the form of revenue balances.

The Council has been presented with a net saving budget proposal for 2014/15 but despite this the financial risks facing it have increased significantly over the past twelve months as the magnitude in reductions in government support become clearer.

Government Grants

The anticipated financial pressures associated with this reduction represents the greatest and most profound financial challenge faced by the Council over the last twenty years and how we react will shape the organisation and its services and the way we supervise them for many years to come.

With the absence of any significant improvement in the wider economic projection the prospect of ongoing reductions in support extends as far as 2017 at a minimum.

In 2010 government grants accounted for 70% of the Council's net funding. By 2014/15 this will be reduced to 50%.

To date the Council has managed to maintain the majority of service provision through a combination of efficiencies, transformation, restructures and income generations. However the Council's net budget has contracted significantly since 2010 (by 21.2%)

and continuing to find savings of this magnitude from a smaller base will become increasingly difficult.

The Council will also consider new income generation opportunities with the aim of providing an income stream which can subsidise essential but non-income generating services.

Having higher working balances at the Council's disposal provides the cushion to enable it to manage the process of reducing the size of the budget. However they should only be used where there is sufficient confidence that the changed programme will be successful.

It is forecast that the Council will be holding balances in excess of the minimum requirement at the end of 2013/14. With the backdrop of potential risk in the budget, the ongoing and expected future challenges facing the Council and the potential need to provide some cushioning, maintaining higher balances against this considerable uncertainty represents a sensible and measured approach.

Business Rate Retention

As highlighted within the section on budget assumptions, from the beginning of this financial year (2013/14) the formula grant system has been based on the business rate retention scheme which includes the revised Revenue Support Grant. Under this scheme Local Authorities still need to operate within the existing national and domestic rate system in terms of their relationships with local business. They still do not have control over how the level of tax is determined for rate payers, i.e. the rateable value of properties or the rate of tax. However, the scheme does allow those Authorities that see increases in their business rates, tax rates and associated revenues to be rewarded. Authorities that have a decline will see a relative reduction in their resources. These calculations are extremely complex.

Under the Business Rates Retention Scheme Councils are able to retain 50% of the real term growth in business rates. Conversely, Councils face the risk of having to absorb 50% of potential decreases. The system includes a levy on disproportionate increases in the safety nets which provide support to limit the impact of significant decreases.

Under the Local Government Finance Act 2012 Councils can form pools for the purpose of business rate retention. This is beneficial if in the period a real term rise in business rates for the sub-region to pool business rates as this means that the levy paid by the District Councils is reduced or eradicated for some of these resources can be retained in the pooling area.

Under the new legislation the Leicestershire Authorities agreed to set up a business rate pool which became operative from 1 April 2013. However, in setting up the pool it was agreed that income and the pool mechanism would be reviewed during the year to ensure there were the benefits envisaged. The legislation allows the business rates pool to be terminated and also if this decision is made the pool can be re-enacted at a later date.

The Business Rate Pool performance has been monitored during the year and the inherent risk in pooling business rates have increased in the last 12 months due to:

- Lack of certainty around rating appeals

- Continued uncertainty around the detailed operation of various aspects of the new regime
- A more negative outlook on perspective business rate outturns amongst Authorities
- The increase in political profile of the burden of business rates on businesses and the increased likelihood that changes adverse to Local Authorities would be introduced.

Given the potential downside, the nature of the pooling calculation means that Authorities may be better off operating individually as they can qualify for “safety net” payments from the Government.

It is difficult to produce reliable estimates on perspective pool outturns for 2013/14 and 2014/15. However, indicative forecasts are deficits for both years. Because of these uncertainties and the high level of risk it was agreed between the Leicestershire Authorities that the pool be terminated for 2014/15. The decision for this Council was determined under delegated powers agreed in setting up the pool by the Chief Executive and Chief Financial Officer in consultation with the Leader and Chair of the Policy, Finance and Development Committee.

Going forward, it is hoped that more clarity on the detailed operation of the business rates regime and the appeals position will emerge enabling a firmer view of the prospects of pooling in 2015/16. Assuming greater clarity is received regarding business rates pooling, the Leicestershire Authorities can re-consider the possibility of a new pool being established for 2015/16 during the summer of 2014.

Under the business rates pooling partnership agreement there is no liability for this Council if the pool does not make a surplus in 2013/14.

Local Council Tax Support

At the Council meeting in January 2013 the Council Tax Support Scheme for 2013/14 was approved. The way council tax support is funded fundamentally changed in 2013/14 with the Government reducing the National funding available by 10%. As the new support scheme is effectively a Council Tax discount, the Council’s tax base has reduced thereby reducing the amount of Council Tax collected. To offset this the Government allocated funding to all Authorities as part of the overall start-up funding assessment for 2013/14.

In addition, the Government provided a transitional grant funding for 2013/14 only to those Authorities who reduce the support to working age claimants by a maximum of 8.5%. This Council received the transitional funding for 2013/14 but for 2014/15 this funding was withdrawn. The Council at its’ meeting on 22 January 2014 considered changes to the current Council Tax support scheme which resulted in support reducing by 15% for working age claimants. This will ensure that this Council and all other precepting Authorities recover the shortfall in funding resulting from the withdrawal of the transitional grant funding.

As with the Business Rates Retention Scheme how Council Tax support is operated and funded imposes significant additional risk on this Council. Any additional growth and support and/or reduction in collection rates over and above what has been seen within our approved scheme and within fixed Government funding will have a direct cost on this Council and all other precepting Authorities. The Council will aim to mitigate these risks. Current projections indicate that the current scheme is operating within the assumptions built into the estimate for 2013/14.

Interest Rate and Capital Investment Decisions

The differential between the current Bank of England base rate and the prevailing rate of inflation is also considered to be a medium term risk in the budget proposals. The current differential will have to be kept under continual review. The cost of borrowing will become a fixed and immovable long term cost within the Council's annual budgets. Any income or efficiencies estimated for capital schemes may be less than expected and therefore this is a risk.

In recognising the risks, capital scheme reports also highlight the mitigation strategies employed by the Council in terms of managing those risks. However the risk cannot be entirely eliminated and therefore the residual risk will need to be managed and accepted.

Demand Growth

Population growth has significantly diminished and in the recent 2011 Census had declined by over 9% since the 2001 Census. However as the housing market recovers linked to the recovery of economic growth it is expected that pressure derived from increased demand for services will return. There is a risk that the Council may not have the resources to meet this increased demand.

Balances

In formulating this budget the recommended minimum level of General Fund revenue balance is set at £660,150. This level of reserve is based on CIPFA's recommendation of a minimum balance of 10% of total net expenditure as reasonable.

With all the uncertainties described above it is this minimum level of General Fund revenue balances that continues to give the confidence to state that the budget proposal is robust.

Reserves and Provisions

The Council maintains a range of funds for specific purposes. These receive contributions from revenue and are also to defray expenditure often on a regular basis.

A major review of all funds has been undertaken by the Chief Financial Officer. This has determined whether balances are still appropriate or there are any significant changes that mean a reserve is no longer required.

The Council's reserves are reducing and therefore because of the challenges facing the Council (like all other local authorities) it is important to maintain an adequate level of reserves.

As Chief Financial Officer I have carried out a review of the reserves. I am proposing that a new Income Profiling Reserve be created. This reserve will be there to cover any potential volatility in some projected fee levels.

Council Tax

Again, the Government has offered a council tax freeze equal to 1% for 2014/15 for all councils that are prepared to hold council tax at existing levels. The Government has more recently confirmed that it will be offering another freeze grant in 2015/16 again equal to 1% with the 2014/15 grant being rolled up into the Revenue Support Grant.

In practice this will not cover the impact of inflation on the budget and will compound the savings target when the grant potentially ends.

All residents have been used to a significant element of funding for services being provided by Central Government. With this being cut dramatically, residents will increasingly become responsible for funding the services they want and need or face the choice of not receiving the services.

Given a free choice some residents would choose not to pay for services they did not use and thus ultimately there will remain a need for taxation to fund some services. The question for the Council to decide is what the correct balance of service provision is versus the correct level of taxation.

However without continued government support for services it is inevitable that either service provision will need to be considerably lower or taxation higher.

Having looked at the budget and the savings that are made I am satisfied as Chief Financial Officer that it is sustainable to accept the government grant and freeze council tax for 2014/15. However the situation will have to be monitored and the Medium Term Financial Strategy when it is reviewed in March 2014 will have to allow for the reduction of grant income in 2015/16 and onwards.

Medium Term Financial Strategy (MTFS)

Considerable effort at Member and Officer level has been directed at establishing a budget framework that covers future years and that links the need to identify savings with the corporate priorities. This has continued to deliver a balanced budget for 2014/15 but considerable financial uncertainty remains beyond that year.

The Council has historically faced up to its financial challenges and I believe will continue to do so in this period of unprecedented constraint.

Steps have been taken and resources have been directed towards the development of a plan to address the projected funding gap in future years.

As highlighted within this report this will continue to require significant business transformation and a radical rethink about what services the council provides and the way in which they are provided. Considerable importance has been attached to this at both Member and Senior Officer levels.

Indicative council tax levels included within the Medium Term Financial Strategy should represent a marker for what is considered affordable in the current economic climate. At these levels of increase there is a key assumption that business transformation would be able to deliver the majority of the savings targets. The Medium Term Financial Strategy is being reviewed and a report will be presented to the Policy, Finance and Development Committee on 25 March 2014.

General fund revenue reserves have been determined taking into account the risks identified within this report and also in the Risk and Sensitivity Analysis for 2014/15 and Forward Forecast to March 2018 (Appendix 5). Therefore the level of balances together with reserves is deemed to represent an adequate level of provision against potential financial risks inherent with the MTFS.

Conclusion

Given the actions taken and the levels of reserves and balances I am therefore of the opinion that the budget proposals for the General Fund have been properly prepared and are realistic in the assumptions made. The proposals have been arrived at after taking appropriate Officer advice and have been recommended for approval by the Planning, Finance and Development Committee and Service Delivery Committee.

John Dickson
Chief Financial Officer and Section 151 Officer
February 2014