

## **ROBUSTNESS OF BUDGET ESTIMATES AND ADEQUACY OF RESERVES**

### **Background**

Section 25 of the Local Government Act 2003 requires the authority's Chief Financial Officer to comment on the robustness of the estimates and the adequacy of reserves allowed for in the budget proposals in the budget report, so Members have advice available to them when they make their budget decisions.

Further, the CIPFA guidance on Local Authority Reserves and Balances states that a statement reporting on the annual review of earmarked reserves should be made to Council, at the same time as the budget. The statement should list the various earmarked reserves, the purpose for which they are held and provide advice on the appropriate levels. It should also show the estimated opening balances for the year, planned additions/withdrawals and the estimated closing balance.

### **Robustness of Estimates**

All Councils face a period of uncertainty in their long term resource planning after 2010/11, as any government after the General Election balances the need to nurse a weak economy back to growth while needing to address an escalating funding shortfall in government finances which is causing a ballooning level of government debt and questions over UK sovereign debt status. The Council is addressing this uncertainty through modelling a range of possible scenarios and starting to prepare medium term strategies to handle the position which emerges after the election. The question of government funding cuts seems to be how much and how soon rather than whether there will be any.

The proposed budget for 2010/11 however is on the safer ground of year 3 of the 3 year settlement announced by the government back in December 2007 which gave the Council a reasonably sound grant position in spite of £5m grant still lost to the area through grant damping. The 2010/11 budget and medium term financial plan has been informed by:

#### 1. Council Wide Risk Management

Risk Management is well embedded across the authority and is an important element of the business planning and budget processes at Strategic, Portfolio and Business Unit levels. Risk workshops and training sessions have been held throughout 2009 at all levels of the authority to ensure that each business and service plan clearly identifies the key risks to the achievement of its objectives. This includes training sessions for Members and employees.

The Risk Management Strategy is reviewed annually and was last updated in November 2008 (the latest update is in progress but slightly delayed due to the Council re-organisation). The Strategy clearly sets out the approach to Risk Management within the authority and identifies roles and responsibilities for all concerned as well as detailing the methodology to be adopted for identifying, assessing and monitoring of risks.

The Council's strategic risk register has also been regularly reviewed throughout 2009 to ensure that it is up to date and relevant, with risks being added, removed and changed where appropriate in full consultation with Directors and Members. In addition, stringent efforts have been made to identify and manage risks and opportunities attached to the many Projects and Partnerships the authority works with.

In reports to Directors and Cabinet, authors are asked to highlight any associated risks and opportunities and how these will be managed – this ensures that all risks are identified and not just the legal and financial implications. Pressures and developments identified during the 2010/11 Service & Financial Planning process focus on the major risk areas for the authority as in previous years and the Council's exposure to risk and risk management is integral to the budget setting process. The latter includes a review of the robustness of the reserves position and modelling of different future government grant reduction scenarios.

## 2. The Monitoring Process

Financial monitoring is carried out on a monthly basis and highlights any significant variances, and therefore areas of risk, both for current and future years, with regular reports being presented to Directors and Cabinet during the year. Performance and risk monitoring are also undertaken regularly to complement the financial monitoring and are formally reported on a quarterly basis to Corporate Management Team and Cabinet. This provides further indications of any potential risk areas for the council and action is taken to review any issues identified.

## 3. The Budget Setting Process

Finance officers meet with budget holders and review all budgets on an annual basis. Budgets are cash limited. Areas of unavoidable growth, pressures and developments have been identified and scrutinised as part of the budget process along with the deliverability of the savings package which forms an integral part of the overall strategy. These link to both the budget monitoring process, performance monitoring and risk management, discussed above, together with other issues such as meeting new legislative requirements and statutory obligations.

## 2010/11 Budget Assumptions:

<u>Inflation</u>	
Pay Award	0% for 2010/11, 2011/12 and 2% for 2012/13. Any actual pay awards will have to be found from within cash limited budgets. Local Authority employers nationally have announced there will be no pay increase offered for NJC staff for 2010/11. As part of a three-year pay deal for teachers a pay increase of 2.45% took effect from 1 <sup>st</sup> September 2008, 2.3% took effect from 1 <sup>st</sup> September 2009 and there is an increase of 2.3% planned for 1 <sup>st</sup> September 2010.
Employer's Pension Contribution	Increases of 1.0% of the paybill in 2010/11, 2011/12 and 2012/13 taking the total contribution to 18.3% A further triennial evaluation of the pension fund based on the March 2010 position, is due to be undertaken shortly which could result in a revision to the figures for 2011/12 and 2012/13. The allocation of any increase in cost between employees and the Council is subject to review as part of national arrangements the scheme as a whole is likely to be reviewed again following the General Election as part of a wider review of public sector pension schemes.
Social Care Purchasing Budgets	The % increase for next year is currently under negotiation with providers. This is a priority service area which has been protected from the general 0% inflation assumption and has also received considerable demographic growth and additional staff funding for children's services.
Electricity, Gas, Water	0% in 2010/11 and 2011/12; 2% assumption for 2012/13
Inflation/Income provision	A provision of £1.5m was earmarked and included in the December report for contractual inflation pressures and potential income shortfalls during the recession such as for PIP rentals, Building Control and Planning Fees. £871k of this has now been allocated and tight control will be exercised to ensure that the remainder is only allocated where a very real need can be proven in priority areas.

Demographic Growth – Adult Social Care	The 2010/11 service and financial planning strategy includes an investment of £1.675m in Adult Social Care arising from inflation, demographic growth and the increasing the demand for care packages.
Children & Families growth	The cost of looked after children has been a key pressure area in 2009/10. The 2010/11 service and financial planning strategy includes an investment of £1.9m to support the provision of social care for Children & Families together with a further earmarked contingency of £0.5m for additional pressures. This investment is for both inflation and increasing service pressures.
Interest Rates	Treasury projections are based on base rate, currently 0.5%, starting to increase in September 2010 and rising to 1.5% in March 2011, 3.5% March 2012 and 4.5% March 2013. Our investment and borrowing strategies for 2010/11 are set within this context. The assumptions for new borrowing are 3.5%, 4% and 4.5% in 10/11, 11/12 and 12/13 respectively and the average return on investments is 2.5%, 3.5% and 5% respectively. One of the primary objectives is to reduce the Council's exposure to risk while at the same time maximising returns. The Treasury Management Strategy for 2010/11 is presented to Council alongside the budget reports.
Treasury Management	Following the collapse of the Icelandic banks and in response to revised guidance issued by CIPFA, the Council has modified its procedures for Treasury Management, to further involve members and in particular to give the Audit Committee responsibility for reviewing treasury policies, procedures and the associated management of risk. The Treasury Strategy for 2010/11 follows the requirements of the Revised CIPFA Treasury Management Code of Practice and clearly identifies the various exposures to risk and strategies in place to minimise this.
Dedicated Schools Grant (DSG)	The figure assumed for Dedicated Schools Grant is £ 102.716m. This is slightly more

	<p>(approx £272k more than the indicative DCSF figure) based on our latest pupil numbers estimate. That part which is delegated to schools will be delegated in line with the agreed schools' local funding formula in line with DCSF guidance. DSG is not finalised until June.</p>
Estimates on the level and timing of capital receipts	<p>The revenue budget and capital programme assume £81m anticipated future capital receipts over the medium term planning period. Any delays in generating expected receipts or in the amounts generated will need to be taken in to account in future service and financial strategies. This could require scaling the capital programme back, re-phasing schemes or entering in to additional prudential borrowing. Delivery of projected receipts is monitored on a monthly basis as part of overall financial monitoring and reported to Cabinet quarterly.</p>
Prudential Borrowing / Prudential Indicators	<p>The Council will make use of the ability to borrow outside the main government funded service allocations, abiding by the Prudential Code and ensuring that such borrowing is appropriate and affordable.</p> <p>Prudential Indicators are approved as part of the budget strategy (see separate report on this agenda) and are monitored and reviewed on a regular basis.</p> <p>The rules around the calculation of the cost of borrowing that must be charged to the revenue account – the minimum revenue provision (MRP) has been prudently applied in setting the 2010/11 budget strategy. The policy in relation to MRP is set out in the Treasury Management Strategy Report. The Council has an ambitious capital investment programme set out in the capital programme report which, if all schemes proceed and are funded as expected, will result in total prudential borrowings of £108m (since April 2004) costing £7.7m pa representing 6.1% of the net revenue budget excluding schools. The impact of the new prudential borrowing, which is included in the 10/11 strategy, is £46.80 per annum for a band B property.</p>
Single Status	<p>The Single Status process is underway and is expected to reach a conclusion during 2010/11.</p>

	<p>Liabilities are potentially incurred from 1<sup>st</sup> April 2007 and provision was made in the 2007/08 and 2008/09 accounts after consultation with the external auditors. The 2009/10 accounts will be closed on the same basis. There is a £2.25m central revenue budget provision projected in the medium term strategy for 2010/11 onwards and a further provision of 4% additional costs within Education –LEA and DSO impacts – schools have also been advised to include a 4% provision. There is possible exposure to liabilities around back pay even before April 2007 but this is difficult to gauge until the process is nearer concluding an overall package. Possible application for a capitalisation direction can also be made for meeting backdated one off costs when there is any information available to support a claim, but the success of this is likely to be limited under the regulations by the assessed availability of in house balances to fund liabilities.</p>
Demand-Led Pressures	<p>The Senior Management Teams and Cabinet are expected to manage in-year demands within existing budgets, by re-prioritising or implementing action plans to ensure that costs are met from the available funding, including any underspends brought forward from previous years. There is a policy that service overspends can be carried forward to future years, but they must then be addressed as top priority.</p> <p>The budget proposals for 2010/11 and future years include reasonable levels of revenue contingency. However, general reserves may have to be used to address unforeseen additional expenditure that cannot be funded elsewhere. It is assumed that the reserves would then be restored in future years to maintain the minimum level of reserves required.</p>
Efficiency Savings	<p>The Senior Management team and other managers, all have a responsibility to ensure the efficient delivery of services and value for money are achieved. Savings of £4.726m were identified during the 2010/11 budget process with a further £0.5m from education, a significant proportion of which could be</p>

	<p>classified as efficiency savings.</p> <p>The Council is also making good progress towards achieving the 3% for 2008/09 and 2009/10 and 4% for 2010/11 cash releasing savings required under the Government's Delivering Efficiency Agenda (National Indicator 179) and an estimate of £4.8m was submitted as the projected NI 179 efficiencies for 2009/10. Delivering Value for Money is integral to the Service &amp; Financial Planning Process.</p>
<p>Financial Risks inherent in any new funding partnerships, major outsourcing deals or major capital developments</p>	<p>There are a number of major capital projects that have been identified which require careful project management and monitoring during 2010/11 and beyond to ensure commitments are matched by funding actually achieved, particularly the reliance on capital receipts and future government funding levels for the council and its public sector partners. These include the Town Centre Redevelopment and Borough Towns Initiative, BTI - Schools &amp; Learning Communities, the Local Housing Investment Programme and New Civic Offices.</p>
<p>The availability of other funds to deal with major contingencies</p>	<p>General reserves may have to be used temporarily and restored if revenue contingencies, management and policy action is insufficient to deal with a major issue.</p>
<p>The overall financial standing of the authority (level of borrowing, debt outstanding, collection of council tax etc.</p>	<p>The Council's approach to sustaining its overall sound financial position is covered in a number of sections of this Appendix already . The overall projected net indebtedness position at 1 April 2010 is £48m; net prudential borrowing anticipated in the medium term strategy is £44.3m which relies on capital receipts totalling £77.1m (in 2010/11 and future years; further information is provided in both the Capital Programme and Treasury Management Strategy Reports). The Council budgets prudently for its level of borrowing, avoiding external borrowing where cash flow permits. The assumed council tax collection rate for 2010/11 onwards is high at over 99%, but being achieved already for past years. This adjustment also allows for additional 'in year' losses such as increased take up of Single Person Discount and other reliefs. For each 1% not collected the cost is approximately</p>

	<p>£0.54m in lost income to the Council. Legislation requires that any collection fund deficit is corrected through Council Tax in the next year.</p> <p>Cumulative collection rates for recent years are (as at October 2009)</p> <table> <tr> <td>2004/05</td> <td>99.48%</td> </tr> <tr> <td>2005/06</td> <td>99.48%</td> </tr> <tr> <td>2006/07</td> <td>99.52%</td> </tr> <tr> <td>2007/08</td> <td>99.34%</td> </tr> <tr> <td>2008/09</td> <td>98.88%</td> </tr> </table> <p>Recovery for all years is projected to be well over 99% finally.</p>	2004/05	99.48%	2005/06	99.48%	2006/07	99.52%	2007/08	99.34%	2008/09	98.88%
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The authority's track record in budget and financial management	<p>The Council continues to demonstrate strong financial management with outturn being within +/- 1% of the net budget set:</p> <ul style="list-style-type: none"> <li>• 2006/07 –underspent by £0.479m (0.47% of budget)</li> <li>• 2007/08 – underspent by £0.300m (0.27% of budget)</li> <li>• 2008/09 - underspent by £0.366m (0.31% of budget)</li> </ul> <p>This demonstrates continued strong financial management, despite considerable pressure on service budgets, notably children's social services.</p>										
The strength of the financial information and reporting	<p>Use of Resources forms part of the Audit Commission Comprehensive Area Assessment (CAA) for Local Authorities and focuses on financial management and its links to the strategic management of the authority. Revised CAA methodology has made it a more challenging test for Local Authorities with more emphasis on value for money and on outcomes for local people. In 2009, the Council scored 2 overall out of a maximum 4 for the new Use of Resources judgement in line with the majority of authorities.</p> <p>Financial monitoring is provided on a monthly basis and budget and closedown reports are consistently prepared within the statutory deadlines.</p>										
Virement and Year End Procedures	<p>The Council has clear rules relating to virement and the carry forward of under/over spends which are set out in the financial regulations.</p>										

	<p>Virement is an important feature of budgetary control. It provides flexibility to adapt expenditure patterns to meet changing needs and objectives, consistent with Council policy.</p> <p>No Head of Service or Business Manager should plan to overspend. All expenditure should be consistent with service and business plans and the overall approved budget. All underspends or deficits on controllable budgets at year end will be carried forward to the next financial year as first call on the budget for the following year.</p>
<p>The adequacy of the authority's insurance arrangements to cover major unforeseen risks</p>	<p>The Council's insurance arrangements are a balance between external insurance premiums and internal funds to "self insure". The Council use the services of an external insurance advisor to provide additional expertise in managing insurance arrangements.</p> <p>The insurance section work closely with the Audit &amp; Risk Manager to identify insurance related risk areas and recommend ways of mitigating future risk.</p>

These assumptions are reviewed on an annual basis.

## **Reserves & Balances Policy**

### **Introduction**

Guidance on local authority reserves and balances is available from the Chartered Institute of Public Finance & Accountancy (CIPFA). This represents good financial management and underpins the framework followed by Telford and Wrekin Council in this policy.

### **Types of Reserves and Balances**

As part of the Service & Financial Planning process, the Council will consider the establishment and maintenance of reserves and balances.

Reserves and balances can be held for a number of purposes. Some reserves and balances are essential for the prudent management of the Council's financial affairs. These will provide a working balance to cushion the impact of uneven cash flows; a contingency for the impact of unexpected events or emergencies and allow the creation of earmarked reserves to meet known liabilities. The consequences of not keeping a minimum level of reserves can be serious and is therefore one of the considerations taken into account when setting the medium term financial plan.

When establishing reserves, the Council will ensure compliance with the Code of Practice on Local Authority Accounting in the United Kingdom (the SORP).

Some of the most commonly established earmarked reserves are:

- Sums set aside for major schemes, such as capital developments
- Insurance reserves – to provide for an element of self-insurance
- Service Balances – to permit year end under spends to be carried forward for future commitments
- School Balances – unspent balances of budgets delegated to individual schools

### **Level of Reserves and Balances**

The minimum prudent level of reserves that the Council should maintain is a matter of judgement. It is the Council's safety net for unforeseen circumstances and must last the lifetime of the Council unless contributions are made from future year's revenue budgets. CIPFA guidance does not set a statutory minimum level so it is up to the Council itself, taking into account all the relevant local circumstances, to make a professional judgement on what the appropriate level of reserves and balances should be. Telford & Wrekin Council will adopt a risk based approach to determine the appropriate level of reserves and balances to sustain and that which can be released to support the medium term financial plans.

Reserves and balances are only maintained in accordance with the risk assessment undertaken and are used in a planned way. Therefore the opportunity cost of maintaining the determined levels is kept to a minimum while interest is earned on the retained amount.

### **Process**

Each reserve and balance will have a clear purpose showing how and when it can be used together with a process for review to ensure continuing relevance and adequacy.

An annual review of reserves and balances will be undertaken as part of the budget process each year and a schedule presenting the estimated opening balances for the forthcoming year, planned additions to/withdrawals from and the estimated closing balances will be presented in the budget report. The schedule will also show the purpose of each reserve and a comment on the appropriateness of the value held.

The key financial risks will also be identified and an assessment of estimated exposure and possible mitigation will be made. This will link to the Council's key strategic risk register. The conclusion of this risk evaluation process will determine the resources available over the medium term to support the Council's budget.

This process will be repeated each year to ensure the ongoing adequacy of the Council's reserves and balances.

### **Responsibilities and Reporting Mechanism**

The Chief Financial Officer has a duty to local tax payers, and must be satisfied that the decisions taken on balances and reserves represent proper stewardship of public funds.

The level and usage of reserves will be formally approved by Council, as part of the budget strategy, informed by the Chief Financial Officer's judgement and expertise.

The budget report to Council will include a statement showing the estimated opening balances for the year ahead (including general fund and earmarked funds), any projected additions to/withdrawals and an estimated end of year balance. This will be accompanied by a statement from the Chief Financial Officer on the adequacy of the general reserves and provisions for the forthcoming year and the authority's medium term financial strategy. A statement reporting on the annual review of reserves and balances will also be made to Council at the same time.

### **Legal Framework**

This policy is in accordance with the following legislation:

Local Government Finance Act 1992 - The balanced budget requirement  
Local Government Act 2003 – The Chief Finance Officer’s duty to report on the robustness and adequacy of reserves when the authority is considering its budget requirement

Local Government Act 1972 – the requirement for each authority to make arrangements for the proper administration of their financial affairs and that the Chief Finance Officer has responsibility for the administration of those affairs