

ROBUSTNESS OF BUDGET ESTIMATES AND ADEQUACY OF RESERVES: STATEMENT OF THE CHIEF FINANCIAL OFFICER

BACKGROUND

A key responsibility of the Chief Financial Officer is to give assurance on the robustness of the budget strategy which includes highlighting the risks associated with its deliverability and sustainability and the adequacy of reserves.

The framework within which the Council's budget setting process operates and the final budget strategy was developed is governed by legislation which provides regulatory safeguards for the Council:

Section 25 of the Local Government Act 2003 requires the authority's Chief Financial Officer to report on the **robustness of the estimates and the adequacy of reserves** allowed for in the budget proposals in the budget report, so Members are informed and can consider this when they make their budget decisions.

Section 114 of the Local Government Act 1988 highlights the Chief Financial Officer's responsibility to report to members if it appears to him that an unbalanced budget is likely to be set for the year.

Local Government Finance Act 1992 identifies the requirement to set a balanced budget.

The Local Government Act 1972 – Section 151 – Financial Administration requires that authorities should appoint a Section 151 Officer to have responsibility for the proper administration of its financial affairs.

The Accounts and Audit Regulations 2003 – Regulation 5 – requires that the accounting records and control systems include measures to ensure that risk is appropriately managed.

The requirements of the prudential Code must also be complied with (a separate report on prudential Indicators is included elsewhere in this suite of service and financial planning reports).

In addition the CIPFA guidance on Local Authority Reserves and Balances requires 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

Overview

Following the Comprehensive Spending Review announcements in October 2010 it was clear that the level of cuts to Government Grant funding for local government would be significant. This was borne out by the grant settlement announcements in December 2010 (for 2011/12 and 2012/13) which left the Council facing real term grant cuts of £40m over the period 2011/12 to 2014/15. More recently, the Chancellor's Autumn Statement in November 2011 re-iterated that the outlook for public finance is not improving and further spending cuts beyond 2014/15 are to be expected. Given this challenging financial position, the Council has been running a comprehensive review of all its services and staffing structures since 2010. The reviews are progressing well with £11.7m gross savings being delivered in 2011/12 and an estimated £19.1m gross savings in 2012/13. Close monitoring will continue throughout the year to ensure that restructuring and service reviews meet the timetables set and savings are delivered. Work will continue to develop additional detailed proposals to deliver the further savings targets set out in the Service & Financial Planning strategy.

Overall therefore, given the continuation of the planned programme of service reviews and accompanying organisational and staff restructures which have been under way for some time now, it is considered that the Council is pursuing a sound financial strategy in the context of the most difficult financial position it has ever faced due to Government grant cuts.

The 2012/13 budget and medium term financial plan has been informed by:

1. Council Wide Risk Management

We are continuing with the planned approach of service reviews but the high level of grant cuts will increasingly have front line service impacts and must be thoroughly impact assessed and final decisions informed by extensive consultation with the community in general but also where appropriate with specific groups of service users. It therefore seems inevitable that the level of financial risk will increase both to individual services and the operation of the council as a whole and this will be common to local authorities across the country. The current review of key risks is thus important to ensure we put in place a level of mitigation wherever possible.

In addition to the £1.6m ongoing contingency, we have set aside a one-off general contingency of £2.145m next year and will seek to add to that with any underspend at the end of 2011/12. A risk based review has also been carried out of all reserves and balances to inform the budget strategy. There has also been an assessment of key service risk exposure resulting in additional revenue investment into Adults' social care services.

Individual service areas have continually managed and monitored key risks relating to their service areas to ensure they are providing the best service they can faced with reduced resources and ongoing reviews. The senior management team monitors service delivery performance and seeks to mitigate significant potential exposures to risks.

2. The Monitoring Process

Monitoring provides a regular financial health-check throughout the year and also provides information which feeds into the budget strategy. Financial monitoring follows a risk-based approach with high-value, volatile areas being monitored more closely than low-value, less volatile areas. Regular reports are presented to Senior Management Team and Cabinet during the year which highlight any significant variances and therefore areas of risk. Progress on the programme of service and staffing reviews will be monitored through this route flagging both 'in year' and future year financial strategy impacts. The reports also monitor the budget contingency and performance against council tax, business rates and sales ledger income collection targets.

3. The Budget Setting Process

The overall medium term financial planning position of the Council is controlled through a model which is updated during the year as new information becomes available - including current year trends identified through monitoring. At a more detailed level finance officers meet with budget holders and review all budgets on an annual basis on top of the usual monitoring work. Budgets are cash limited. Areas of unavoidable growth and pressures 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.

2012/13 Budget Assumptions and Considerations:

Given the difficult financial position the Council faces, a tight line has been taken on planning assumptions for next year but this is mitigated by the inclusion of the additional one-off general contingency (currently £2.145m which will be increased at year end) and a risk assessed review of reserves and balances.

<u>Inflation</u>	
Pay Award	There is no allowance included for pay awards. There is an indication, in The Chancellor's Autumn statement, of a 1% increase in 2013/14 and 2014/15 and the planning assumption is that service areas would meet this cost within cash limited budgets if this was the case. No increases are planned for teachers pay.
Employer's Pension Contribution	The Council agreed with pension fund officers and the fund's actuaries the maintenance of its contribution rate of 16.3% for the 3 years 2011/12 to 2013/14. Following the independent review of public services pension provision undertaken by John Hutton the Government is proposing changes to the scheme and a number of options are currently being consulted on with a proposed implementation date of 2014.
Employer's National Insurance Contribution	Nil increase
Non-Pay budgets	3% in 12/13 and 2% in 13/14 and 14/15 – this is being held centrally and will only be allocated to services based upon demonstrated and agreed need.
Contingencies	There is an ongoing general contingency of £1.6m which is being supplemented in 2012/13 by a one-off £2.1m; any underspend at the end of 2011/12 will also be carried forward to 2012/13 as additional, one-off contingency (so the total one-off contingency may total up to £4m on current projections).
Service Pressures	The key service pressures identified for the medium term relates to the cost of Adult Social Care Packages and Children's Social Care.

	<p>Additional ongoing funds of £2.5m are being invested into Adult Social Care in 2012/13 in order to meet increasing demands and the impact of Continuing Health Care costs being displaced onto the Council. Discussions are ongoing with the PCT about the potential to review the allocation of these cases between the PCT and the Council and one-off contingencies to support Adult Care Services. There are also savings totalling £4.1m to be delivered from Care & Support in 2012/13 so overall there is a net dis-investment of £1.6m.</p> <p>There is a plan to radically change service delivery within Adult Social Care which includes a major service re-design, moving more towards re-ablement and independent living.</p> <p>In line with national trends, numbers of Children in Care continue to increase; further there has been an increase over the medium term in the length of time that children remain in care; both lead to significant financial pressures and have resulted in a significant overspend against the budget in the current financial year. Our longer term strategy for Children & Families is to provide more support at the very early stages of difficulties and providing more intensive, targeted help for families with more complex needs. Progress in delivering against the reduced budget for 2012/13 will be monitored very closely. In recognition of the pressures facing the Safeguarding Service and to help deliver the savings required, it has been agreed to defer savings from restructuring until 2015/16.</p>
<p>Central Government Funding / Local Government Resources Review</p>	<p>The Government is changing the way local government is funded and a new Business Rates Retention Scheme will operate from 2013/14 onwards. The Council supports the general principles of the change however there are some potential risks that are highlighted in section 4.2 of this report. The Council has responded with comments on the proposed scheme through the consultation process. The proposals have many elements and it is not possible to make an assessment of the financial impact. Therefore funding projections</p>

		beyond 2012/13 have a very significant degree of uncertainty and will be updated as soon as further information becomes available.
Welfare Reforms	Benefit	The Council currently administers the nationally prescribed housing and council tax benefit schemes and receives a subsidy payment from the Department of Works and Pensions in relation to benefits paid out, together with a grant towards the administration costs of the scheme. The Government is proposing changes to the Welfare Benefit System and the council tax benefit scheme is to be replaced with a local discretionary council tax rebate scheme in April 2013 with Government support cut by 10%. This equates to £1.4m for the Council. The Government's assumption is that a new scheme will be in place from 2013/14 but this has been identified as an unacceptably high risk given that the details of how a new scheme will operate will be governed by regulations that may not be released until the Autumn and software suppliers are stating that there will be little time to make necessary changes to systems. The Council's budget assumption is therefore that a new scheme will be operational by 2014/15.
Interest Rates		<p>Base rates began the year at 0.5% and have remained there all year. The Bank of England has extended its Quantitative Easing programme to £325bn. The next move in the base rate is expected to be upwards but not until late 2014. Our investment and borrowing strategies for 2011/12 are set within this context.</p> <p>The assumptions for new borrowing are 1.5%, 1.75% and 3.0% in 12/13, 13/14 and 14/15 respectively. The current strategy is to use maturing investments to reduce the need to borrow and therefore interest rate exposure. The average return on investments is 4.21% in 2012/13, 4.31% in 13/14 and 3.65% in 15/16. 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 2012/13 is presented to Council alongside the budget reports. The investment portfolio is monitored on a regular</p>

	<p>basis and advice is received from independent professional treasury advisors. An investment that generated a high rate of return was redeemed during 2011/12 in order to reduce the risk rating of the overall investment portfolio.</p>
Treasury Management	<p>The Treasury Strategy for 2012/13 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. The Audit Committee has a role to review and monitor the Council's treasury management arrangements which includes policies, procedures and the management of risk. The 2012/13 Treasury Strategy was presented to Audit Committee on the 31 January for their consideration and comments.</p>
Dedicated Schools Grant (DSG)	<p>The figure estimated for Dedicated Schools Grant was £110.380m at the time of writing this report. The final DSG allocation to the Council will not be known until June 2012 when all adjustments for academies and pupil numbers are finalised. The Government is currently consulting on changes to the funding arrangements for schools and a shadow settlement is expected in 2012/13 which will show potential allocations resulting from the reforms. The earliest implementation date for a new funding system is 2013/14.</p> <p>Current consultation indicates that the Government does not intend to claw back any further monies from Local Authority Formula Grant in 12/13 to fund academies and therefore the General Fund budget will not be impacted. However, any schools transferring to academy status during the year will result in a reduction in Dedicated Schools Grant.</p> <p>Going forward, any further transfers to academy status are likely to have an adverse impact on the Council's Formula Grant. It is unclear as to the precise methodology to be implemented by the DFE and therefore the impact.</p>
Estimates on the level and timing of capital receipts	<p>The revenue budget and capital programme assume around £110m anticipated future capital receipts over the medium term planning</p>

	<p>period. Any delays in generating expected receipts or in the amounts generated will need to be taken into 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. There should be no further decisions taken which significantly increase this medium to long term exposure until there is a clear pattern of receipts being delivered as planned and satisfactory progress with the programme of service and staffing reviews is sustained.</p>
<p>Prudential Borrowing / Prudential Indicators</p>	<p>The use of prudential borrowing is in line with the capital programmes approved by full Council. The 100 day review of the 2011/12 budget reduced outstanding debt significantly which will generate ongoing savings of £2.9m. Given the overall financial position faced by the Council it is important that no further significant prudential borrowing commitments are entered into (unless matched by additional savings/income flows) until delivery of the savings from the service and staffing review programmes is substantially secured.</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) - have been prudently applied in setting the 2012/13 budget strategy. The policy in relation to MRP is set out in the Treasury Management Strategy Report.</p>
<p>Single Status</p>	<p>The Single Status process is underway with an implementation date of April 2014. An annual provision equal to 4% of the relevant pay bill has been set aside in the accounts for the 4 years 2007/08 to 2010/11. It is now considered that there is adequate funding in the provision and no further contribution will be made. The additional ongoing budget is included in the</p>

	<p>budget strategy wef. 2014/15 in line with the implementation date although has been reduced to reflect the reduced risk by the movement of employees on fixed points to salary grades and the reduction in the workforce of around 20%.</p> <p>There is possible exposure to liabilities from back pay and equal pay claims and the authority will seek to identify the possible range of liability at similarly structured authorities though this is limited especially at present. Possible application for a capitalisation direction can 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.</p>
Savings	<p>There is a planned programme of service reviews and restructures which will deliver savings over the medium term planning strategy. Gross employee savings of £9.6m and non-staff savings of £9.5m have been identified for 2012/13. Additional gross savings of £1.1m and £12.5m respectively are budgeted for 2013/14 and 2014/15. There is a reserve set aside to meet redundancy costs and commitments against this are being monitored as restructures progress; the position will be reviewed at year end. The Council has also been successful in its application for a capitalisation direction totalling £2.9m for 11/12 which can be used to fund the statutory element of redundancy costs incurred in year. A risk review has also been undertaken on all 2012/13 savings to identify those with high risks and action plans will be developed for these which will be closely monitored. Further, there are action plans for all procurement savings which are being monitored by the Procurement Steering Group.</p>
Financial Risks inherent in any new funding partnerships, major outsourcing deals or major capital developments	<p>There are a number of major capital projects that have been identified which require careful project management and monitoring during 2012/13 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</p>

	the Town Centre Redevelopment, Borough Towns Initiatives and Building Schools for the Future.								
The availability of other funds to deal with major calls on contingencies	General reserves or other funds may have to be used temporarily and restored if revenue contingencies, management and policy action is insufficient to deal with a major issue. The Council has evaluated the risks it faces against available balances as outlined earlier in this appendix and concluded that around £3.7m is available to use in the overall budget strategy at the start of 2012/13; the proposed strategy recommends the use of £1.4m leaving £2.3m. This position will be kept under review.								
The overall financial standing of the authority (level of borrowing, debt outstanding, collection of council tax etc.	<p>The Council's approach to sustaining its overall sound financial position is covered in a number of sections of this Appendix. The overall projected net indebtedness position at 1 April 2012 is £79.2m; net additional prudential borrowing anticipated in 12/13 is £32.5m; this reduces in future years due to capital receipts being received. The total reliance on capital receipts in the medium term strategy is £110m in line with profiled disposals (additional 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 and running down investment exposure while new placement rates are low.</p> <p>The assumed council tax collection rate for 2012/13 onwards is high at over 99%, but being achieved already for past years. For each 1% not collected the cost is approximately £0.56m in lost income to the Council. Legislation requires that any collection fund deficit is corrected through Council Tax in the next year. Collection has outperformed projections allowing use of a council tax surplus as part of next year's strategy.</p> <p>Cumulative collection rates to date for recent years are</p> <table border="0"> <tr> <td>2008/09</td> <td>99.41%</td> </tr> <tr> <td>2009/10</td> <td>99.38%</td> </tr> <tr> <td>2010/11</td> <td>98.89%</td> </tr> <tr> <td>2011/12*</td> <td>63.58%</td> </tr> </table>	2008/09	99.41%	2009/10	99.38%	2010/11	98.89%	2011/12*	63.58%
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	<p>Recovery for all years is projected to be well over 99% finally.</p> <p>*to-date</p>
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"> ● 2006/07 –underspent by £0.479m (0.47% of budget) ● 2007/08 – underspent by £0.300m (0.27% of budget) ● 2008/09 - underspent by £0.366m (0.31% of budget) ● 2009/10 – underspent by £0.332m (0.27% of budget) ● 2010/11 – underspent by £0.083m (0.07% of budget) <p>This demonstrates continued strong financial management, despite considerable pressure on service budgets, notably children's social services.</p>
Virement and Contingencies	<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 Service Delivery Manger should plan to overspend. All expenditure should be consistent with approved service priorities and the overall approved budget.</p>
The adequacy of the authority's insurance arrangements to cover major unforeseen risks	<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 Council's Risk Officer 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.

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 adopts 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.