

Committee: Cabinet

Agenda Item

Date: 16 February 2017

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Title: Robustness of Estimates and Adequacy of Reserves

Portfolio Holder: Councillor Simon Howell

Item for decision

Summary

1. As part of the annual budget setting process, the Section 151 Officer is required to give the Council formal advice on the robustness of estimates and the adequacy of reserves. This is so Members can set a budget in full awareness of the risks and uncertainties, and ensure that adequate contingency reserves exist.
2. The advice, known as the "Section 25 report", is being considered by Cabinet tonight and then by Full Council on 23 February as part of the budget approval process.
3. The Scrutiny Committee reviewed the budget reports on 7 February. Comments from the Committee are in a separate item on the agenda.

Recommendations

4. The Cabinet is requested to approve, for recommendation to Full Council:
 - a) That the Council takes account of the advice in the report when determining the 2017/18 General Fund budget and Council Tax.
 - b) That the Council approves the risk assessment relating to the robustness of estimates as detailed in the report
 - c) That the Council sets the minimum safe contingency level for 2017/18 at £1.280 million.
 - d) That the attached Reserves Strategy is adopted.
 - e) That the Council agrees that no transfers to or from the Working Balance should be built into the 2017/18 budget.

Financial Implications

5. No direct implications arise from the recommendations.

Background Papers

None.

Impact

Communication/Consultation	A comprehensive budget consultation exercise was undertaken with in excess of 800 responses
Community Safety	No specific implications
Equalities	No specific implications
Health and Safety	No specific implications
Human Rights	No specific implications
Legal implications	The report is prepared in order to comply with Section 25 Local Government Act 2003
Sustainability	No specific implications
Ward-specific impacts	No specific implications
Workforce/Workplace	No specific implications

Section 25 report

6. Section 25 of the Local Government Act 2003 requires each local authority, when setting its annual General Fund budget and level of Council Tax, to take account of a report from its Section 151 Officer on the robustness of estimates and adequacy of reserves. This document is the report made under Section 25 by the Director of Finance and Corporate Services, as UDC's Section 151 Officer, applicable to the setting of the General Fund budget and Council Tax for 2017/18.
7. The purpose of this requirement is to ensure that when deciding on its budget for a financial year, a local authority is formally made aware of any issues of risk and uncertainty by the Section 151 Officer. The local authority is then expected to ensure that its budget provides for a prudent level of reserves to be maintained.
8. The Director of Finance and Corporate Services has assessed that the minimum safe contingency level for the Working Balance is £1.280 million. This sum is calculated using the following formula
(Total gross service expenditure + total gross service income + capital financing costs + investment income + recharge to HRA + HRA share of corporate costs) x 2%
2017/18 working balance reserve equates to;
$$\begin{aligned} & \text{£}35,423,000 + \text{£}23,973,000 + \text{£}1,861,000 + \text{£}65,000 + \text{£}1,507,000 + \text{£}293,000 \\ & = \text{£}63,122,000 \times 2\% = \text{£}1,262,000 \text{ (this calculation uses rounded figures, the} \\ & \text{actual working balance is } \text{£}1,266,000 \end{aligned}$$
9. Section 26 of the Act empowers the Secretary of State to set a minimum level of reserves for which a local authority must provide in setting its budget. Section 26 would only be invoked as a fallback in circumstances in which a local authority does not act prudently, disregards the advice of its Section 151 Officer, and is heading for financial difficulty.

Basis of advice for the Section 25 report

10. In forming the advice for this report, the Director of Finance and Corporate Services has considered the following:

- The requirement established in the Council’s Medium Term Financial Strategy to ensure that a safe level of contingency is maintained.
- The degree to which the Council’s financial plans are aligned to the Council’s statutory obligations, local priorities and policy objectives.
- The adequacy of the information systems underpinning the Council’s financial management processes.
- Risks associated with the Council’s activities, as identified within the risk register.
- The level of earmarked and unearmarked reserves within the General Fund.
- The degree to which uncertainties exist within the draft 2017/18 budget.

Robustness of Estimates

11. There has been detailed scrutiny, review and challenge of budgets by managers, finance officers and CMT. The aim has been to ensure that the budget is based upon realistic estimates, for example, ensuring that contractual commitments are provided for, salary budgets reflect the approved establishment and current staff in post, and income budgets are based on an assessment of price and demand.

12. No budget can ever be completely free from risk. Necessarily, assumptions are made which means that the budget will always have an amount of uncertainty. The analysis below sets out the major risks applicable to 2017/18 and an indication of the possible impact.

13. It is not possible to give a precise estimate of the impact of each identified risk. As a general guide, the following broad definitions have been used:

Probability	Low	Possible, but unlikely
	Medium	Probable
	High	Almost certain
Impact	Low	Possible variance of £5,000 to £20,000
	Medium	Possible variance of £21,000 to £50,000
	High	Possible variance of over £50,000

Risk item	Probability	Impact	Overall Risk of budget variance
<p>Waste & Recycling – This continues to be one of the most complex financially and at greatest risk of volatility. Fuel costs and disposal costs, particularly around cost of dry recycling disposal are variable. Other budget risks have been identified regarding trade waste and green waste, all of which have income budgets that depend upon accuracy of forecasting activity levels. The Council maintains a Waste Management reserve to mitigate the risk. The budget is based on current disposal costs</p>	Medium	High (adverse or favourable)	Medium
<p>Local Plan – Additional consultancy spend or resources may be needed in order to take forward the Local Plan process; however the Planning Reserve exists to meet additional costs. Due to recruitment issues the need for agency staff has increased and these are at a higher cost than substantive posts.</p>	Medium	High (adverse)	Medium
<p>Planning appeals. A risk of costs of defending appeals and the meeting of costs awarded against the planning authority. The current position of the Local Plan process raises the risk levels in this area.</p>	Medium	Low (adverse)	Medium
<p>Business Rates Appeals. The way in which Business Rates is accounted for increases the risk around the forecasts. The key area of risk still remains with appeals; the 2017 reset of business valuation could lead to further appeals.</p>	Medium	Medium (adverse)	Medium
<p>100% Business Rates Retention. Due to the uncertainty of the increased responsibilities and the precise funding mechanism, it is still difficult to predict the financial implications of the new scheme.</p>	High	High (adverse or favourable)	High
<p>Efficiency Savings. Work continues to find ways of achieving the same or improved outcomes at lower cost. It is probable that some savings opportunities will be realized with unbudgeted savings arising in 2017/18. In addition, the budget includes costs for Service Redesign and Organisational Development; these will be funded from the Transformation Reserve. It is still possible that unbudgeted costs will arise. Where budgets have already been reduced because of identified savings, the revised budget level is untested so there is an inherent risk of adverse variances.</p>	Medium	Medium (adverse or favourable)	Medium
<p>Commercialisation. Creation of Council wholly owned subsidiaries and other income generating projects. This is in the early stages and the outcomes are expected to generate increased income to support the council with the funding reductions.</p>	High	High (favourable) Low (adverse)	High

Risk item	Probability	Impact	Overall Risk of budget variance
<p>Car Park Income. The budget is based on the existing tariff and charging periods as detailed in the fees and charges section of the budget report. If at some point during the year the Council decides to make changes, this will affect the income. For example if the charging period is shortened, or if the Christmas/New Year free periods are continued, income will reduce.</p>	Medium	Low (adverse or favourable)	Medium
<p>Fees & Charges income. If economic conditions deteriorate or demand fluctuates there may be unbudgeted loss of income. Building Control, Planning, Land Charges, Licensing, Lifeline and Food Imports are all income streams where risk of volatility has been noted.</p>	Medium	Low (adverse)	Medium
<p>Treasury management. Investment risks are spread between public and private sector counterparties including UK banks systemically important to the UK economy. In the unlikely event of a banking failure, there could be a serious impact on the Council.</p>	Low	High (adverse)	Medium
<p>Reforms to Housing & Council Tax Benefit. The Council has approved a Local Council Tax Support Scheme that will require non-vulnerable working age people to pay more Council Tax than previously. The Council has reduced its commitment to subsidise the LCTS scheme for Town and Parish councils. This is based on estimates and subject to variation.</p> <p>Housing benefit reforms and benefit caps have had an adverse impact on amount of claimants benefit awards and this could have an impact on collection rates and increased claims for discretionary housing payments.</p>	Medium	Medium (adverse)	Medium
<p>Universal Credit – This was due to commence in early 2015/16 but was delayed and only started in late 2015/16 and further roll out is not expected until late in 2017/18. Implications of delay are primarily around the Working Balance level.</p>	Medium	Low (adverse or favourable)	Medium
<p>External funding. Due to inherent uncertainty about local authority budgets, there is a risk that funding for services such as the Highways Ranger could be reviewed or reduced.</p>	Medium	Low	Low
<p>Supplies & Services contracts. Where contracts have indexation clauses, estimates have been made of the inflationary increase that will be applied. In addition some contracts are due to be re-tendered during the year which could affect the base price. Accordingly there is an inherent risk of price volatility.</p>	Medium	Low (adverse or favourable)	Low

Risk item	Probability	Impact	Overall Risk of budget variance
<p>Capital Financing costs. These are influenced by variable factors such as cash flow, variations in the Capital Programme and availability of capital receipts. In some circumstances greater revenue financing of capital expenditure may make economical sense over the longer term.</p>	Medium	Low (adverse or favourable)	Low

14. Taking all of the above issues into consideration, the Director of Finance and Corporate Services is unable to provide a full assurance that there will be no unforeseen variances. This is an expected and acceptable situation for any organisation that has to deal with a large number of variables. Provided that the minimum safe level of balances is maintained (as set out in the attached Reserves Strategy), any variations arising as a result of any lack of robustness in the estimates should be manageable.

15. The risks identified will be proactively monitored and mitigating action taken as soon as reliable trends emerge. Budget monitoring reports to Members during the financial year will set out the latest position and action being taken, where applicable.

Adequacy of reserves

16. Attached is the Reserves Strategy which sets out the purpose, risks and calculation for each reserve held by the council.

17. It is the opinion of the Director of Finance and Corporate Services that the reserves as set out in the Strategy are adequate and appropriate.

Risk Analysis

Risk	Likelihood	Impact	Mitigating actions
<p>Actual events may differ from the assumptions and estimates used to produce the draft budget, which will lead to variances from the budget.</p>	<p>4 (variances will occur requiring action to be taken)</p>	<p>3 (potential impact which could adversely affect the council's financial position if not managed)</p>	<p>Budget monitoring and corrective action taken as necessary. Maintain sufficient reserves and Working Balance.</p>