

Committee: Cabinet

Agenda Item

Date: 16 February 2016

10

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 25 February as part of the budget approval process.
3. The Scrutiny Committee reviewed the budget reports on 9 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 2016/17 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 2016/17 at £1.234 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 2016/17 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 2016/17.
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 £1,234,000. 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%
 This for 2016/17 equates to

$$£33,695,000 + £23,800,000 + £2,497,000 + £119,000 + £1,331,000 + £335,000 = £61,777,000 \times 2\% = £1,235,540$$
 (this calculation uses rounded figures the actual outcome is £1,234,000)
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 2016/17 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 2016/17 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 up to £100,000 |
| | Medium | Possible variance of £100,000 to £250,000 |
| | High | Possible variance of over £250,000 |

| Risk item | Prob-ability | Impact | Overall Risk of budget variance |
|--|--------------|-----------------------------------|---------------------------------|
| <p>a) Waste & Recycling – This continues to be one of the most complex financially and at greatest risk of volatility. Fuel costs 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. With the price of oil at a six year low the cost of disposing of dry recyclables has increased significantly. The budget is based on current disposal costs</p> | High | High (adverse or favourable) | High |
| <p>b) Localisation of Business Rates. The way in which Business Rates is accounted for increases the risk around the forecasts. However a review in the summer of 2015 now enables the council to use a realistic forecast rather than using the minimum guaranteed amount.</p> | Medium | High (adverse or favourable) | Medium |
| <p>c) 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 2016/17. In addition, the budget does not include the implementation costs that may arise, on the basis that these will be funded from the Transformation Reserve. Therefore it is probable 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>d) Car Parks 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 there is a repeat of Christmas/New Year free periods, income will reduce.</p> | Medium | Low (adverse) | Medium |
| <p>e) 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>f) 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 |

| Risk item | Prob-ability | Impact | Overall Risk of budget variance |
|--|--------------|--------------------------------|---------------------------------|
| g) 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. | Low | High (adverse) | Medium |
| h) 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 committed to subsidise the LCTS scheme to ensure cost neutrality for major precepting authorities. This is based on estimates and subject to variation. | Medium | Low (adverse) | Low |
| i) Universal Credit – This was due to commence in early 2015/16 but was delayed and only started in late 2015/16. Implications of delay are primarily around the Working Balance level. | Medium | Low (adverse) | Medium |
| j) Local Plan – Additional consultancy spend or resources may be needed in order to take forward the Local Plan process. The Planning Service has budgets for the majority of this work; however the Planning Reserve exists to meet additional costs. | Medium | Low | Low |
| k) Fritch Green Community Centre. Risks have been identified with the Fritch Green community centre. This issue is unresolved and the Council may be required to incur further costs before the facility is transferred to the parish council. | Medium | Low (adverse) | Low |
| l) 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. | Medium | Low | Low |
| m) 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. | Medium | Low (adverse or favourable) | Low |
| n) 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. | 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 |
|---|---|---|--|
| In general, actual events may differ from the assumptions and estimates used to produce the draft budget, which will lead to variances from the budget. | 4 (variances will occur requiring action to be taken) | 3 (potential impact which could adversely affect the council's financial position if not managed) | Budget monitoring and corrective action taken as necessary. Maintain sufficient reserves and Working Balance. |