



Council – 27 February 2013

Report by Chief Finance Officer on Robustness of Budget Estimates and Adequacy of Reserves

Purpose of report

To advise the Council on the robustness of the estimates in the budget and the adequacy of the proposed financial reserves before recommending to Council the Council's Medium Term Financial Strategy 2013/17, the Revenue Budget for 2013/14, Capital Programme 2013/23, Reserves levels and Treasury Management Strategy 2013/14.

1.0 Background

- 1.1 Section 25(1) of the Local Government Act 2003 requires that the Chief Financial Officer (Section 151 Officer under the Local Government Act 1972) reports to the Council when setting its Council Tax on (a) the robustness of the estimates in the budget (b) the adequacy of the proposed financial reserves.
- 1.2 Section 25(2) of the 2003 Act requires the Council to have regard to this report in approving the budget and Council Tax.

2.0 Context

- 2.1 The Council is setting its budget at a time when it faces significant challenges. In broad terms these can be split into 3 categories; economic, local government and local challenges. Each of these challenges are explored below:

- 2.2 Economic Challenges

The UK economy, along with the rest of the developed world, continues to be faced with little or no growth in the near term and the threat of a triple dip recession.

- 2.3 Local Government Challenges

As a result of the Government's austerity measures Local Government in the UK is working in an environment of delivering significant savings. This follows the Spending Review 2010 (SR10) which identified a 28% reduction in real terms for local government funding. In January 2013 councils received notification of their funding allocations for the last two years of SR10. The level of reduction for 2013/14 was in line with that announced in SR10. However, an additional 1% reduction would be applied in 2014/15. The Chancellor also indicated in the Autumn Statement that austerity measures would continue until at least 2018, rather than 2015 as previously indicated.

In addition to the continued austerity measures councils are implementing significant changes to Government policy from April 2013, including the localisation of council tax support and technical reforms to council tax discounts & exemptions. A further change is the introduction of the Business Rates Retention Scheme, where councils retain a proportion of additional business rates locally. On the face of it this is a positive step. However, it does present additional risk to councils if business rates reduce and funding allocations are also less certain. Looking ahead the next Government policy change will be the introduction of universal credit.

All of these changes present significant risks to the Council over the period of its Medium Term Financial Strategy (MTFS).

2.4 East Northamptonshire Challenges

As noted above the Council faces significant external challenges that it will need to manage over the medium term. In February 2012 the Council agreed a MTFS which addressed a number of specific financial challenges I was faced with when joining the Council, including an unfunded capital programme, an unsustainable revenue budget with an over reliance on reserves to balance the budget each year, and reducing reserves.

During 2012/13 the Council has made good progress in delivering its MTFS.

However, there are still a number of actions that are in the process of being implemented (e.g. sales of assets), further savings are still required in the future and there are new risks to manage. As I mentioned last year the MTFS is only a plan. The biggest challenge will be for the Council to deliver it.

3.0 **Medium Term Financial Strategy (MTFS) 2013/14 to 2016/17**

3.1 The MTFS is a key part of ensuring the Council's future. During the 2012/13 budget planning round, the MTFS received a substantial refresh to ensure the stability and sustainability of the Council's finances over the medium term. The approach during the 2013/14 budget planning round has been to update the previous years MTFS for any changes to assumptions, local policy changes, national policy changes and known risks. Councillor involvement in this refresh has been through the Finance Sub Committee meetings in November 2012 and January 2013, as well as a Member Budget Workshop held during December 2012.

3.2 Assumptions

Section 5 of the Budget Report presented to the Policy and Resources Committee on 11 February 2013 sets out all of the assumptions which underpin the MTFS. These assumptions are robust and are based on the most up to date intelligence available. However, as with any assumption, there is an element of risk that the reality will be different. The following assumptions in the MTFS contain the most risk:

- **Government funding** via Revenue Support Grant (current assumption is as per notified Government allocations and a 7.5% reduction per annum from 2015/16). The Government funding for 2013/14 has been confirmed and for 2014/15 has been provisionally set. However, the funding from April 2015 has the potential to change significantly as a result of the next Spending Review due in Autumn 2013.
- **Business Rates Retention.** The current assumption is for the level of business rates in 2013/14 to grow to £21.3m, from a baseline of £19.3m. The Council is likely to retain around £0.4m with a further £0.170m generated by "pooling" with other councils in Northamptonshire. The actual level of business rates for 2013/14 will not be known until after the end of the financial year. This presents the Council with a new risk to manage, as previously all Government funding was certain at the time of setting the budget. This risk is being managed by a proportion of the anticipated increase being held in an earmarked reserve until the amount is clear. Beyond 2013/14 no further growth in Business Rates is factored into the MTFS. The Council is currently developing an approach to forecasting its level of Business rates over the medium term.
- **Localisation of council tax support (CTS) and council tax technical reforms (discounts & exemptions).** The current assumption is that the shortfall arising from the "10% reduction" in Government funding for CTS in 2013/14 will be met from council tax discounts/exemptions, the CTS transitional grant and an 8.5% council tax liability for those entitled to CTS. Beyond 2013/14 it is assumed any additional costs arising from reduced government funding are mitigated by reductions to the CTS scheme.
- **Universal credit.** The picture for implementing universal credit is starting to emerge. However, the implications for the Council's finances still remain unclear.

- **Council tax** (current assumption is an increase of £5 in 2013/14 with 2% per annum thereafter & no local referendum). The MTFS assumes the Council will increase its council tax to the maximum level without it being considered as “excessive” by the Government and without triggering a local referendum. Whilst the Government has published the criteria for the level above which council tax increase is considered “excessive” for 2013/14, it has not done so for future years. The Government has indicated it will review, and may change, the level in future years. This will need to be reviewed on an annual basis by the Council.

If the Council adopts a different strategy it will not only need to identify further savings to bridge any increased funding gap, but also to mitigate the additional risks (e.g. lower reserves) it will place on the MTFS.

- 3.3 Across the period of the MTFS the level of savings required to be delivered are £1.8m per annum. The majority of these are in 2013/14 (£0.7m), each of these is a specific proposal within the budget and each has a clear plan about how it will be delivered. However, in years 2-4 of the MTFS a further £1.1m of savings still need to be identified. The Council needs to identify and develop plans on how these will be achieved. This work needs to commence immediately following the setting of this budget. A good start in identifying these additional savings is already in place and a number of areas are already under review. Based on the relatively small level of further savings to be identified, the profile across years 2-4 of the MTFS and the track record in delivering savings over the past 3 years, the Council should be confident these will be achieved.

3.4 Delivering the MTFS

The MTFS requires a number of key deliverables to be achieved and implemented in order to achieve a stable and sustainable financial position for the Council. Key deliverables include implementing savings plans, identifying further savings, selling assets and increasing revenues by encouraging more businesses into the district. As noted in Section 2 of the report all of these will need to be managed against a backdrop of further significant change to the Local Government sector. To ensure delivery the Council is advised to ensure that:

- project teams are established to deliver the savings programmes, particularly those still to be identified, and that these teams are resourced to the right level.
- progress against savings plans are regularly monitored, with variances and any mitigating actions reported to Finance Sub Committee.
- members take future decisions that support the aim of maintaining a financially stable and sustainable Council as set out in the MTFS, including a clear funding source.

3.5 The Long Term Financial Position

As noted in Section 2 of the Budget Report to Policy & Resources Committee on 11 February 2013 the long term financial position for the Council continues to show costs increasing at a faster rate than funding. The potential “gap” between expenditure and income could be £3m per annum in 10 years time based on the assumptions used. The Council will need to be cognisant of this position when making strategic and policy decisions in the future. The likely solutions to this shortfall will be around increasing revenues through the Business Rates Retention scheme by growth in the number of businesses in the district and reducing costs by operating more efficiently, effectively and innovatively.

4.0 **Revenue Budget 2013/14**

- 4.1 The revenue budget 2013/14 is the first year of the Council's four year MTFS. The budget has been developed using a robust process with officer and member involvement.

4.2 Budget Process

An important feature of the budget process is that Heads of Service are responsible, with the support of finance staff, for the preparation and determination of their income and expenditure estimates. The active involvement of Heads of Service in determining their spending plans and income generation estimates ensures ownership of the budget and that the officers responsible for delivery of the services are happy that financial targets are achievable. During the 2013/14 budget cycle all items within the base budget have been challenged by Corporate Management Team (CMT) and any changes to the figures submitted have only been incorporated with the acceptance of the Head of Service. The arrival of the Finance Manager has also provided resource to challenge current practices, improve the budgeting process and provide assurance around the robustness of budget estimates.

4.3 Members have been involved in the budget process through the Finance Sub Committee, who have challenged the proposals, and Member Budget Workshops.

4.4 Budget Proposals

The budget includes £698k of savings, many of which have already been delivered as part of the in-year savings programme for 2012/13. The remaining savings proposals are considered to be low risk in terms of delivery. However, there are a couple of proposals which merit specific mention due to their risk:

- Nene and Pemberton Centre additional income. This proposal is based on investing capital monies into the leisure offering which is anticipated to generate additional membership income of £150k in 2013/14 rising to around £400k per annum by 2015/16. The risk is that the additional income does not materialise at this level. However, extensive work has been undertaken to mitigate the risk including a report by external leisure consultants on the potential opportunity and risk sensitivity around likely funding streams, the commencement of improvement works at the Nene Centre, the imminent commencement of works at the Pemberton Centre, the minimisation of disruption to income streams during the works (e.g. provision of a gym in Members Room and continued, albeit slightly disrupted, service at Pemberton Centre) and regular meetings with CCP during the transition period. Despite these mitigations this proposal carries a higher than normal level of risk for 2013/14. This is due to a number of uncertainties, including timely completion of the improvements works and levels of expected demand for the new facilities performing in line with forecasts. As such there will be close monitoring of the financial progress of this proposal during the year.
- Planning income. The planning income budget target has been reduced by £150k to reflect current levels of demand for planning activities and bring the income budget in line with the historic average.

5.0 **Draft Capital Programme 2013/14 to 2022/23**

5.1 The Capital Programme agreed by Council in February 2012 underwent a major review to focus it on the highest priority areas of capital investment and is fully funded. A key element to the future of the funding position for the Capital programme was the generation of around £5m of capital receipts by selling surplus assets.

5.2 There has been steady progress in the sale of surplus assets programme. It is expected that during 2013/14 the Council will realise, in terms of value, the majority of the assets identified as surplus. This would be ahead of the assumptions included in the MTFS 12 months ago. It is also still envisaged the total level of monies to be raised will be in line with those assumed 12 months ago. However, given the current state of the economy, and specifically the housing market, the Council need to be aware there continues to be risks in both the timing and level of capital receipts forecast to fund the programme.

- 5.3 During the last 12 months the focus on the Council's capital spending has come to the fore with major investments in repair and improvement works to the Nene & Pemberton Leisure Centres and the cessation of the Car Scheme. To provide a greater focus and transparency on capital investment the governance arrangements are being improved for capital planning, monitoring and the control environment. The capital investment plans for the Council are being divided into a Capital Programme, which contains those schemes where costs and funding are certain, and a Development Pool, which contains those schemes in their early stages of development.
- 5.4 The following risks continue to exist in the capital programme and Council needs to be aware of them:
- As noted above the programme assumes around £5m of capital receipts will be realised by selling surplus assets. To mitigate this risk of the expected timing / level of receipts temporary borrowing will be utilised to fund any difference in cash flows.
 - Borrowing to finance the capital programme and development pool. To finance the capital investment plans the Council will be required to borrow monies for the first time since the housing stock was sold over 10 years ago. This presents new risks to the Council in terms of interest rates, refinancing, maturity of loans and being able to service the capital financing costs. The borrowing will be both temporary, to mitigate any cash flow timing difference in capital receipts being realised, and permanent, to finance long term assets. These risks will also be managed through the Council's Treasury Management Strategy (see Section 6 below).

6.0 Annual Treasury Management Strategy 2013/14

- 6.1 The Council's Treasury Management Strategy has been updated to reflect the latest borrowing requirements of the capital programme, latest interest rate forecasts and to update the credit criteria to reflect the changing banking environment whilst ensuring the security of the Council's investments continues to be maintained.
- 6.2 Forecasting the Council's future borrowing and lending costs is always a challenge, but even more so in the current climate of economic volatility and uncertainty. Nevertheless the Treasury Management budget does reflect the capital financing costs to support the approved capital programme and rates of return on investments at this time. The base rate is forecast to remain at its historical low further into the medium term and the budgets will be regularly monitored.

7.0 Forecast Reserves and Balances

- 7.1 Members will be aware that reserves have been used extensively in previous years to finance the deficit on the revenue budget and to fund the capital programme. In response to this the MTFS approved in February 2012 planned to reduce the reliance on reserves to finance the revenue budget from over £1m in 2011/12 to nil by 2015/16. At the same time the Capital Programme would utilise its remaining reserves and replace this funding stream with capital receipts by utilising the Council's surplus assets. This was a key element of the MTFS to ensure the Council's finances remain stable and sustainable in these times of austerity. As noted in the Budget Report elsewhere on this agenda the Council has made good progress in reducing its reliance on reserves. The MTFS assumes no reliance on reserves. This places the Council in a better position than it faced 12 months ago. However, there are still a number of significant risks which I have referred to earlier in the report that still face the Council and need to be mitigated with an appropriate level of reserves.

7.2 Use of Reserves to Finance Spending

The MTFS assumes the level of reserves fund the revenue and capital budgets as follows:

- Revenue – from 2013/14 there is no planned requirement to fund revenue spending from reserves. This is 3 years earlier than planned and should be seen as a major achievement in ensuring the Council's finances are stable and sustainable. It reflects the Council's focus on reducing its costs and being more efficient in the use of its revenue budget.
- Capital - the current capital reserve is due to be fully utilised in 2013/14.

7.3 Minimum reserves

The minimum level of reserves as assessed after considering the risks facing the Council over the medium term is £2m. The £2m consists of two component parts, namely:

- An underlying minimum level of £1m for the long term, and
- In the short to medium term, a minimum level to £2m to reflect the uncertainties currently facing the Council. These uncertainties include Nene Centre roof, the delivery of a cost reduction programme to ensure on-going revenue spending is sustainable, generation of additional income from leisure centre investment, new risks around the implementation/early operation of recent Government policy changes (business rates retention, localisation of council tax discounts/exemptions and council tax support), the introduction of universal credit and planning related activities.

The additional £1m to cover short to medium term risks should be reviewed, along with the underlying minimum level, on an annual basis.

8.0 **Conclusion**

- 8.1 Provided the Council carefully considers and acts upon the above analysis, and officers robustly manage the implementation of the Revenue and Capital Budgets, a positive opinion can be given under Section 25 of the Local Government Act 2003 on the robustness of budget estimates and the level of reserves.

9.0 **Equality and Diversity Implications**

- 9.1 There are no equality and diversity implications arising from this report. Separate assessments will be produced as savings plans are developed over the period of the MTFS to deliver the savings yet to be identified.

10.0 **Legal Implications**

- 10.1 There are no legal implications arising from the report.

11.0 **Risk Management**

- 12.1 This report by its nature considers risk management from a financial perspective.

12.0 **Financial Implications**

- 12.1 The report is of a financial nature and the implications are set out within the report.

13.0 **Corporate Outcomes**

- 13.1 The Corporate Outcomes that the MTFS seeks to help deliver are:

- Good Quality of Life
- Good Value for Money
- Effective Management
- High Quality Service Delivery
- Strong Community Leadership

14.0 Recommendation

- 15.1 That Council carefully consider the content of this report prior to recommending the approval of the Council's Medium Term Financial Strategy 2013/17, the Revenue Budget for 2013/14, Capital Programme 2013/23 and Treasury Management Strategy 2013/14.

(Reason: To ensure the Council complies with statute in setting its Budget.)

Legal	Power: Local Government Finance Act 1992, Local Government Acts 1972, 2000 & 2003, Localism Act 2011				
	Other considerations: Constitution				
Background Papers: Reports To Finance Sub Committee and P&R; precept notifications					
Person Originating Report: Glenn Hammons, Chief Finance Officer. Tel: 01832 742267 ghammons@east-northamptonshire.gov.uk					
Date: 11 February 2013					
CFO		MO		CX	