Appendices
1

NORTHAMPTON BOROUGH COUNCIL

CABINET REPORT

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

AGENDA STATUS: PUBLIC

Cabinet Meeting Date:	19 February 2014
Key Decision:	No
Within Policy:	YES
Policy Document:	YES
Directorate:	Management Board
Accountable Cabinet Member:	Cllr A Bottwood
Ward(s)	N/A

1. Purpose

1.1 To advise the Cabinet on the robustness of the estimates in the budget and the adequacy of the proposed financial reserves for the General Fund and Housing Revenue Account before recommending to Council the Council's Medium Term Financial Plan 2014/19, the Revenue Budget for 2014/15, Capital Programme 2014/19, Reserves levels and Treasury Management Strategy 2014/15.

2. Recommendations

2.1 That Cabinet recommend to Council to carefully consider the content of this report with regards to the General Fund and Housing Revenue Account prior to recommending the approval of the Council's Medium Term Financial Plan 2014/19, the Revenue Budget for 2014/15, Capital Programme 2014/15 and Treasury Management Strategy 2014/15.

3. Issues and Choices

3.1 Report Background

3.1.1 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:

- the robustness of the estimates in the budget.
- the adequacy of the proposed financial reserves.

3.1.2 Section 25(2) of the 2003 Act requires the Council to have regard to this report in approving the budget and Council Tax.

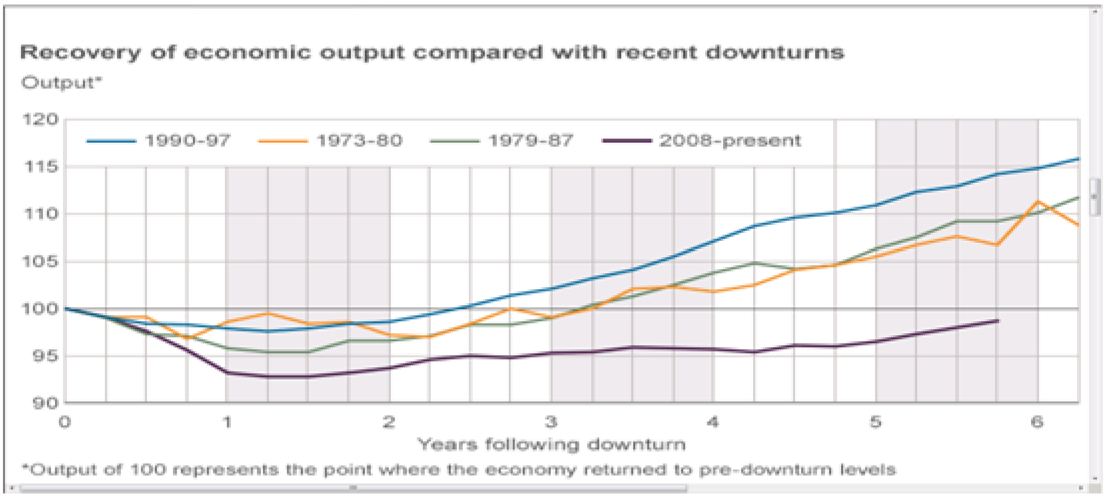
3.2 Context

3.2.1 The Council is setting its budget at a time when it continues to face significant challenges. In broad terms these can be split into 3 categories; economic, local government and local challenges. Each of these challenges is explored below.

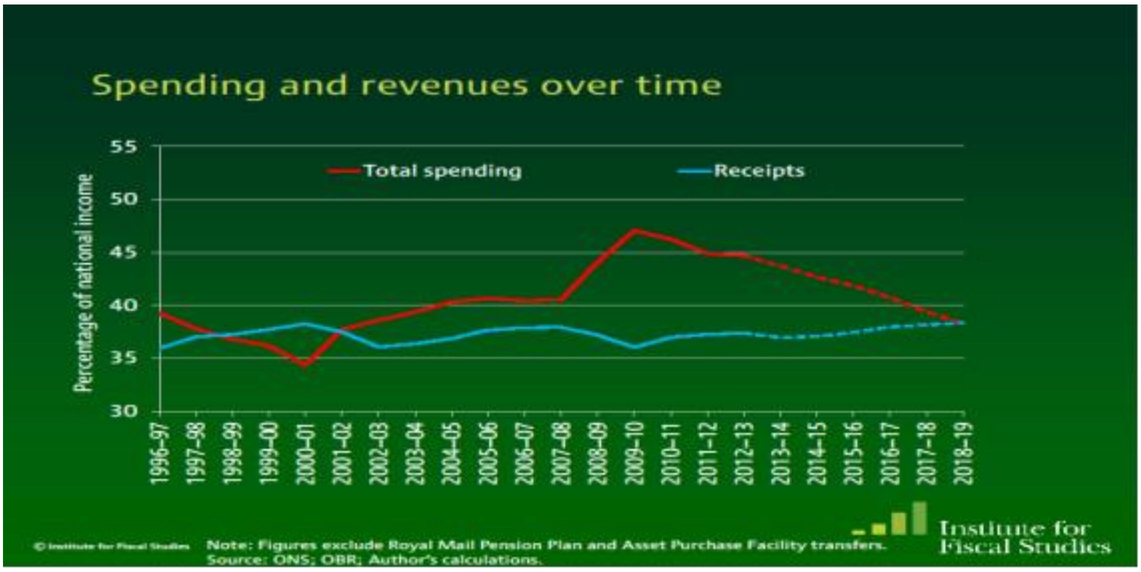
Economic Challenges

3.2.2 The UK economy over the last 12 months has returned to growth. In 2013 the annual growth in Gross Domestic Product (GDP) was 1.9%. This is the fastest rate of growth since the financial crisis in 2008 and the introduction of austerity measures in 2010. This growth is expected to continue in 2014 with the Office for Budget Responsibility forecasting growth at 2.4%.

3.2.3 Whilst this is positive news the UK economy is still below the level of GDP seen in 2008. The period of recession and economic stagnation has lasted significantly longer than similar recent downturns. As can be seen in the graph below it took between 2-3 years to return to the level of GDP in previous downturns. It is likely to take 6 years in the downturn which commenced in 2008:



3.2.4 The UK economy is still operating with an annual deficit and the Government has stated its commitment to a balanced budget by 2018. Due to the depth of the downturn this is longer than previously envisaged. The graph below from the Institute of Fiscal Studies (IFS) shows how the UK income receipts could increase and public spending is likely to continue reducing over the next 5 years.



Local Government Challenges

3.2.5 As announced by Government in their Budget, Spending Round and Autumn Statement during 2013 the austerity measures for the public sector, including Local Government will continue until at least 2018, rather than 2015 as previously indicated. This follows the Spending Review 2010 (SR10) which identified a 28% reduction in real terms for local government funding. In January 2014 councils received notification of their funding allocations for 2014/15 and an illustrative funding settlement of 2015/16. These confirmed that decreases in funding from Government are set to continue for the next two years at the rates seen over the last 4 years.

3.2.6 In addition to the continuing austerity measures councils have implemented significant changes to Government policy, including the localisation of council tax support, technical reforms to council tax discounts & exemptions, keeping council tax increases to a minimum and Business Rates Retention Scheme. Looking ahead the next Government policy change will be the introduction of universal credit and a continued reform of the welfare system.

3.2.7 From these changes it appears that Government are moving slowly away from the previous needs based funding of the old formula grant, towards a system where councils are rewarded for growth in house and business numbers. For example Revenue Support Grant (RSG) is forecast to reduce at significant rates over the medium term and is therefore unlikely to be a primary source of funding for the Council in the future. It is being replaced by New Homes Bonus and Business Rates Retention, both of which reward those areas which can promote and deliver growth.

3.2.8 All of these changes present significant risks, as well as opportunities, to the Council over the period of its Medium Term Financial Plan.

Northampton Challenges

3.2.9 As noted above the Council faces significant external challenges that it will need to manage over the medium term. Over the past two budget planning rounds the Council has implemented a financial strategy which addressed a number of specific financial challenges faced by the Council.

3.2.10 During 2013/14 the Council has made good progress in delivering its Medium Term Financial Plan. The primary areas being:

- Delivery of revenue budget savings and operating within its revenue budget for 2013/14; and
- Changes in terms and conditions and a senior management restructure.
- The transfer of support services to LGSS which is expected to deliver substantial savings over the next five years.

3.2.11 There are still a number of actions that need to be delivered in the future given the increasing revenue funding pressures that, as noted above, look set to continue into the medium to long term. An example of the change and investment programme the Council is in the process of delivering includes the transfer of the Council's housing stock to an Arms Length Management Organisation (ALMO).

3.2.12 In addition to the existing externally driven funding pressures, there are additional calls on Council funding to implement schemes and provide loans in order to promote and enhance the local economy and allow a sound base for future economic growth. The success of this strategy could lead to additional revenue funding becoming available to the Council in the future form of retained growth through Business Rates Retention Scheme and funding arising from the building of new dwellings through the New Homes Bonus grant, however this does give rise to additional pressures in the short to medium term.

3.3 Medium Term Financial Plan 2014/15 to 2018/19

3.3.1 The Medium Term Financial Plan is a key part of ensuring the Council's future. The approach during the 2013/14 budget planning round has been to update the previous year's plans for any changes to assumptions, local policy changes, national policy changes and known risks. This has then been used as a basis to identify savings requirements for the years 2014/15 to 2018/19.

Risks and Mitigations

3.3.2 General Fund Revenue

a) There are £1.4m of savings to be achieved in 2014/15 onwards; those currently identified are itemised in the budget report at appendix 5. Specific ones of notes are:

   - Restructures / staffing savings of £875k.
   - Printing review of £150k rising to £250k in future years.
   - Employment Costs £365k.

   The risk of delivery of these will be mitigated through the use of a budget tracker to monitor progress; outputs from this will be regularly reported to Management Board and senior councillors.

b) A number of significant reviews will be undertaken during year. These include:

   - Private sector housing;
   - Housing restructure

- Call care
- GF/HRA recharges review

The risk of delivery of these will be mitigated through the use of a tracker to monitor progress; outputs from this will be regularly reported to Management Board and senior councillors

c) The Council is committed to create an Arms Length Management Organisation (ALMO) to deliver the Council's landlord function, plus other housing functions yet to be defined. This will be financed through a management fee paid by the Council to the ALMO. There is a risk of financial implications to the Council arising from the calculation of the management fee or through commitments made to stakeholders through the ALMO creation process.

The risk of this is mitigated through the governance structures and the involvement of the Chief Finance Officer and his representatives in those governance structures.

d) Through the Business Rates Retention Scheme, the Council retains a proportion of the net growth outside the Waterside Enterprise Zone for its own purposes. There is a risk that the forecasts of this business rates growth may not be achieved resulting in lower revenue streams than anticipated.

This risk is mitigated through the inclusion of 50% of the projected uplift in 2014/15 budgets. There are also plans to improve intelligence gathering and information sharing between planning, revenues & finance combined with more detailed modelling of future projections including risk and sensitivity analysis.

e) Through the Business Rates Retention Scheme, the Council retains all the growth from the Waterside Enterprise Zone which is earmarked (through a memorandum, of understanding) for use on South East Midlands Local Enterprise Partnership (SEMLEP) priorities. There is a risk that the forecasts of this business rates growth may not be achieved resulting in lower revenue streams than anticipated; this risk affects Northampton Borough Council via some of the loans to improve Enterprise Zone Infrastructure whereby the funding of principal and interest repayments are expected to come from business rates uplift; if this uplift does not occur, the responsibility for repayment remains with the Council.

This risk is mitigated through modelling of business rates uplift on a site by site basis. There are plans to further improve intelligence gathering and information sharing between planning, revenues & finance combined with more detailed modelling of future projections including risk management and more detailed sensitivity analysis. However, it should be noted this risk is unlikely to materialise until after the end of our MTFP period.

f) Business rates revaluation is planned for 2017 in England and Business Rates Retention Scheme rebasing is planned for 2018. Both of these could impact on projected business rates growth and have a consequent effect on Council revenues.

The risk of these impacts is medium term and is mitigated as per d) above and will be mitigated through liaison with the Valuation Office and monitoring developments in this area.

g) There are some services which historically have had higher levels of financial risk associated with them, including car parking and waste contract.

There is now reduced risk relating to car parking income due to using improved data for producing improved financial forecasting; the costs of the waste contract are being continually monitored and contract risks dealt with through the contract management team.

3.3.3 General Fund Capital

h) There are a large number of high profile capital schemes to deliver over next two years.

A new Capital Programme Board has been introduced to manage the capital programme and improve governance.

i) The Greyfriars bus station is programmed for demolition in late 2013/14 to early 2014/15.

Risks around the residual costs of this scheme are being managed through the risk assessment of reserves and working balances.

j) There is significant capital investment relating to investment in improved infrastructure in the Enterprise Zone. Initial funding of this is from various sources including the Growing Places Fund; repayment of the funding is reliant on business rates uplift.

This risk is managed as per e) above.

3.3.4 Housing Revenue Account

k) A review is being undertaken of recharges between the General Fund and Housing Revenue Account. There is a risk of additional costs falling in the Housing Revenue Account arising from this review.

Any additional costs will be built into the HRA 30 year business plan and the overall finances will managed within that context.

l) The Council is committed to create an Arm's Length Management Organisation (ALMO) to deliver the Council's landlord function, plus other housing functions yet to be defined – see c) above for details.

3.3.5 Housing Revenue Account - Capital

m) There are a large number of high profile capital schemes to deliver over next two years, including the improvement of council housing upto the Decent Homes Standard and Northampton Standard.

A new Capital Programme Board has been introduced to manage the capital programme and improve governance.

3.3.6 Treasury Management

n) The Council has and is entering into a number of loan agreements with local partners.

Risks are fully assessed and loan agreements put into place to mitigate the risks including proposed repayment schedules; interest rates are charged on the loans to mitigate state aid implications.

o) There is a risk relating to interest rate increases.

The interest budgets have been built using latest forecasts of interest rates provided by the Council's risk management advisors, Capita Treasury Services.

3.3.7 Financial Awareness & Skills

p) It is recognised that with the financial challenges and risks the Council faces there is a need for improved financial awareness and improved finance skills amongst budget managers.

The risk of this is being managed through implementing a comprehensive finance improvement plan to include a training programme to raise awareness, providing budget managers with improved financial systems and a review of key financial processes.

Delivering the Medium Term Financial Plan

3.3.7 The Medium Term Financial Plan 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. This will need to be managed against a backdrop of further significant change within 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.
- money used to support these programmes must be on an invest to save basis, with clear criteria and expectations of return.
- progress against savings plans are regularly monitored, with variances and any mitigating actions reported.
- members take future decisions that support the aim of maintaining a financially stable and sustainable Council.

The Longer Term Financial Position

3.3.8 The medium to long term financial position for the Council continues to show costs increasing at a faster rate than funding. By 2018/19 there is projected to be a £6.6m gap between expenditure and income and this could get wider over the longer term using current projections. The Council will need to be mindful of this position when making strategic and policy decisions in the future. Mitigating factors for this could be around increasing revenues through the Business Rates Retention scheme by growth in the number of businesses in the borough, although there are risks around this as noted above, and will be by reducing costs by operating more efficiently, effectively and innovatively.

3.4 Revenue Budget 2014/15

The Financial Position

3.4.1 The revenue budget 2014/15 is the first year of the Council's five year Medium Term Financial Plan. The budget has been developed using a robust process with officer and member involvement.

Budget Process

3.4.2 An important feature of the budget process is that Directors and 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 Directors and 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 2014/15 budget setting cycle, all items within the base budget have been scrutinized and any changes to the figures submitted have only been incorporated with the acceptance of the Directors and Heads of Service.

3.4.3 Councillors have been involved in the budget process through the Overview and Scrutiny Committee, who have investigated and challenged the proposals and Audit Committee who conducted a risk review of the budget proposals.

Budget Proposals

3.4.4 The budget includes £1,365k of savings, delivery of which will need to be managed.

Council Tax

3.4.5 Freezing the Council tax has been a key policy objective for the Government and there is to be a Council Tax freeze grant for the fourth year running. Again the terms are less generous than the first round. There is a grant equivalent to 1% of Council Tax payable for two years, only for councils freezing or reducing Council Tax in 2014-15. 2011-12 was the first year of the Freeze Grant and the additional resource was built into the funding baseline for subsequent years. However, for 2012-13 the freezing of Council Tax was supported by a one off grant of 2.5% of Council Tax. This dropped out of funding in 2013-14 creating a funding gap requiring an equivalent reduction in spend.

3.4.6 The Government has stated Council Tax freeze grants will be incorporated into the baseline for future funding settlements. However, there remains a lack of 100% certainty on the inclusion of the 2013-14 freeze grant, equivalent to 1% of Council Tax in future base funding. The MTFP assumes it is included in base funding in future years, and any future freeze grants will also be included..

3.4.7 The Budget 2014/15 and MTFP 2015/19 has recommended a Council Tax freeze in each year This will need to be reviewed on an annual basis in light of the financial position of the Council and in response to the threshold set by Government to trigger a referendum.

Council Tax Support

3.4.8 Council Tax Benefit reforms were put in place from April 2013 which provided for decisions on benefits to be made at a local level. These reforms did, however, come with a target reduction of 10% in the overall benefits bill. This has been a challenge for local authorities with a number of previous Council Tax Benefit claimant categories exempt from the reduction, and hence there has also been a need to take advantage of flexibility around Council Tax discounts. There was a likelihood that there would be an impact on collection rates as well as general uncertainty in the first year of the new arrangements. Collection rates have actually held up better than anticipated and th council is continually reviewing its scheme on an annual basis.

3.5 Draft Capital Programme 2014/15 to 2018/19

3.5.1 Historically the Council's General Fund Capital Programme has been funded from capital receipts, capital grants, prudential borrowing financed from service revenue savings and prudential borrowing that is affordable within the overall revenue position. This remains largely the case, although New Homes Bonus income is now also being used to finance regeneration and economic growth related projects.

3.5.2 Over the period of the Medium Term Financial Plan, the General Fund Capital Programme is projected to be financed from £8.093m capital receipts. There are risks around the delivery of this level of capital receipt, however the majority of this funding (£7.126m) is planned to be used in 2015/16 and 2016/17. Progress on the achievement of this level of receipt will therefore be closely monitored through the Corporate Asset Board, with any amendments to capital programmes and financing through new Capital Programme Board.

3.5.3 There is £6.750m of funding provided through the, Growing Places Fund and Local Infrastructure Fund which is to be repaid from the Enterprise Zone business rate uplift; risks around the repayment of this are being managed as per 3.3.2 e) above.

3.5.4 The Housing Revenue Capital Programme is funded within the context of overall Housing Revenue Account resources and in line with the stock condition survey and the HRA 30 year business plan. Where there are changes in the overall resources available to the HRA, the capital plans are amended accordingly. In this context there is not a high financial risk relating to HRA capital expenditure, however significant reductions in capital investment would impact heavily on service delivery and put delivery of landlord obligations at risk.

3.6 Treasury Management Strategy 2014/15

3.6.1 The Council's Treasury Management Strategy has been updated to reflect the latest borrowing requirements of the capital programme, latest interest rate forecasts and updated for the credit criteria to reflect the changing banking environment whilst ensuring the security of the Council's investments continues to be maintained.

3.6.2 Forecasting the Council's future short term 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.

3.7 Forecast Reserves and Balances

3.7.1 The previous strategy has been to hold relatively high levels of earmarked reserves to mitigate against the risks foreseeable in the short to medium term. This approach has been reviewed this year and a fundamental review of earmarked reserves and working balance has been undertaken. The new approach is to manage more risk within the risk assessment of the working balance. This results in a lower overall level of reserves needed when compared to the levels of risk than the previous methodology. This is primarily because the new approach, although it recognises all risks, also recognises that not all risks will emerge at the same time if they emerge at all. This means that the levels of overall reserves can be lower.

Minimum Levels of Working Balance

3.7.2 The risk assessed minimum level of balances for 2014/15 is £4.9m, an increase of £1.8m on previous levels. This increase will be managed from the reduced levels of earmarked reserves. The risk assessed minimum level of balances increases for 2015/16 by £0.4m to £5.3m due primarily to increased risks around loans to local organisations. This increase for 2015/16 will also be managed from the reduced levels of earmarked reserves.

3.7.3 The underlying minimum level of working balance necessary to mitigate against short to medium term risks will be reviewed, along with the levels or earmarked reserve, on an annual basis.

Use of Earmarked Reserves

3.7.4 There is a net contribution from earmarked reserves within the 2014/15 revenue budget of £1.464m. This is made up as follows: -

	£m
Increase to Minimum Working Balance	-1.828
New Homes Bonus (NHB) receivable in 2014/15	2.794
Use of NHB	-2.255
Use of Housing and Planning Delivery Grant	-0.175
Net Contribution <u>from</u> earmarked reserves	-1.464

3.7.5 The Housing and Planning Delivery Grant reserve is used to finance specific costs within the planning department.

3.7.6 New Homes Bonus receivable in year, in line with previous years, is transferred into earmarked reserves. Regeneration and economic development schemes to the value of £2.255m have been identified to be funded from the NHB earmarked reserve. This includes £224k to pay for the ongoing revenue costs of prudential borrowing. In addition to this, £2.136m of the NHB earmarked reserve is being used to directly finance capital schemes.

3.7.7 In recognition of the future General Fund revenue pressures, rising to a budget gap of £6.6m in 2018/19, an earmarked reserve of £1.2m for invest to save schemes has been set up. The use of this reserve will be based on a strict criteria linked to a business case and will require sign off by the Chief Finance Officer and the Cabinet Holder for Finance and will only be used for projects which contribute overall to closing the projected budget gap in the short to long term.

3.8 Conclusion

3.8.1 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.

3.8.2 However, it should be noted:

- Whilst risk does exist the estimates are robust both in respect of the underlying estimates and the future deliverability of potential reductions.
- From a Chief Finance Officer perspective there is always a desire to have a high level of reserves to protect against the unknown. However, against the backdrop of reduced public finances, the need to protect service, especially the most vulnerable in the community and provide investment for future growth the level of reserves is currently considered adequate.
- That the Council faces significant financial pressures, particularly in its General Fund Revenue Budget, over the medium term. Over this period the Council must ensure it takes the necessary action to ensure a continued stable and sustainable financial position is maintain.

3.9 Choices (Options)

3.9.1 Section 25(2) of the Local Government Act 2003 requires the Council to have regard to this report in approving the budget for both the General Fund and the Housing Revenue Account.

4. Implications (including financial implications)

4.1 Policy

4.1.1 The revenue and capital budgets are set in support of the Council's priorities and in order to do this effectively, the calculations used within the budgets must be robust; this report demonstrates that, in the opinion of the Chief Financial Officer, the budgets for 2014/15 are robust within the parameters outlines in this report.

4.1.2 Protecting the Council's medium to long term financial position and ensuring adequate provision for reserves allows the Council to continue to deliver services in line with its priorities.

4.2 Resources and Risk

4.2.1 The report is of a financial nature and the implications are set out within the report. This report by its nature considers risk management from a financial perspective.

4.3 Legal

4.3.1 The Council has a legal duty to set a balanced budget each year, bearing in mind its fiduciary duties to the taxpayer, and the HRA is not allowed to go into deficit by law. 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 the robustness of the estimates in the budget and the adequacy of the proposed financial reserves.

4.3.2 Section 25(2) of the 2003 Act requires the Council to have regard to this report in approving the budget.

4.4 Equality

4.4.1 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 MTFP to deliver the savings yet to be identified.

4.5 Consultees (Internal and External)

4.5.1 Internally heads of service and budget managers have been consulted, and Management Board has carried out a detailed challenge of the budget with Members.

4.5.2 The draft capital and revenue budgets were subject to public consultation and the HRA budget was presented to tenants on 4th February 2014.

4.6 How the Proposals Deliver Priority Outcomes

4.6.1 Consulting on the draft budget is a key ingredient of effective financial governance, which contributes to the priority of making every pound go further.

4.7 Appendices

None

5. Background Papers

5.1 General Fund Budget Report

5.2 HRA Budget Report

5.3 Prudential Indicators Report

5.4 Treasury Management Strategy Report

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