



REPORT OF:	DIRECTOR OF FINANCE AND IT
TO:	FINANCE COUNCIL
DATE:	27th FEBRUARY 2017

SUBJECT: The Robustness of the 2017/18 Budget and the Recommended Level of Reserves

1. PURPOSE OF THE REPORT

Section 25 of the Local Government Act 2003 places a statutory requirement on the Council's Chief Financial Officer to report on:

- a) the robustness of the estimates within the overall budget, and
- b) the adequacy of the proposed level of financial reserves

In setting the Budget for 2017/18, Council is required to have regard to this report when making its budget decisions.

2. RECOMMENDATIONS

An overall assessment of the current budget and the assumptions on which this is based, as well as future budget proposals, savings plans and activity forecasts, has identified that whilst there are risks, the overall budget provisions are considered sufficient to meet the Council's legal responsibilities and obligations.

A review of risks, mitigations and contingencies has also been undertaken alongside the review of reserves and provisions.

Finance Council is recommended to consider the assessment by the Director of Finance and IT of;

- the robustness of the Revenue Budget and Capital Programme for 2017/18 (as outlined in the report of the Executive Member for Resources) and
- the adequacy and recommended level of proposed financial reserves (detailed in **Section 5.2** below).

3. RATIONALE

The information provided below is to assist Members in their review of the overall Revenue Budget and Capital Programme and to provide assurance to them that financial advice has been provided throughout the budget setting process.

4. POLICY IMPLICATIONS

The Budget Strategy reflects the corporate priorities of the Council and policy requirements at both a corporate and a departmental level.

5. FINANCIAL IMPLICATIONS

5.1 Robustness of the 2017/18 Budget

5.1.1. Budget Strategy

The Council's overall framework for its medium term budget is contained within the Medium Term Financial Strategy (MTFS). Although the strategy would normally extend over the 3 years beyond the end of the budget year, i.e. to 2020/21, given that Central Government is currently developing mechanisms to significantly change the way Councils are funded from 2020 onwards, the MTFS focuses on the period to 2019/20 until more clarity is provided on the changes over the next 12 months.

The strategy provides for Council-wide involvement with an integrated approach to the preparation of soundly based capital and revenue plans and the associated strategies of managing risk and internal control. Together this ensures effective financial management and governance.

5.1.2 Budget and Tax Setting Process

The annual budget preparation and tax setting process involves the development of robust medium term revenue forecasts and capital plans. In any financial year, the level of Government funding, additional cost pressures (including inflation, service specific pressures and areas of investment and growth), together with an increasing demand for services, necessitates a re-appraisal of service delivery and identification of efficiency savings to address any funding shortfall in order to deliver a balanced budget. The Budget Strategy and proposals submitted have been formulated to reflect these issues.

Throughout the formulation of the Budget Strategy, Portfolio Executive Members have been advised by the Chief Executive, the Deputy Chief Executive and Directors in relation to the operational requirements around policy and legislative initiatives. Likewise, the Director of Finance and IT and senior finance representatives have advised on financial impact and provided comprehensive input to demonstrate financial viability throughout the process. In doing so, and to ensure the robustness of the budget and the budget setting process, we have been mindful of;

- Availability of reliable information;
 - we have sought to ensure that the budget is based on the most up-to-date and realistic assumptions (for example government and Bank of England forecasts for pay and price increases and interest rate movements)
 - assumptions relating to future levels of government funding are based on the Local Government Finance Settlement and predicated on the most recent government announcements.
- Council's guidance and strategy;
 - the Council's Constitution which contains a clear Budget and Policy framework

- the Council's Budget Strategy and approach to budget setting which is clearly defined and communicated
 - consultation with residents, partners and businesses within the Borough and targeted engagement with service users
- Corporate approach and integration;
 - service departments have identified budget pressures and risks at an early stage in the process and have clearly demonstrated realistic service plans linked to the budget resource available
 - the system of cash limited budgets for each Portfolio provides a transparent and accountable arrangement to budget setting; the allocated cash limit takes account of service specific cost pressures and inflation and also includes an apportionment of corporate cost pressures from which each Portfolio has had to formulate a strategy to deliver savings and ensure a balanced budget.
 - The Council's 'early action' approach to meeting both the immediate and forecast financial challenges has been effective in providing a level of resilience to address the Central Government funding reductions over the period to 2019/20. All of the savings relating to the 3 year savings programme of £26.0m approved by Council Forum in September 2014, the £3.6m in-year budget savings programme of 2016/17, together with the £15.0m savings programme developed during 2016/17 and approved by Policy Council on 1st December 2016, have been reflected in the budget.
 - Flexibility;
 - mechanisms to review options for service delivery are linked into the budget process
 - flexibility to free up resources to deliver service improvement and to deliver the Council's priorities
 - flexibility in budget management as included within the Council's Constitution

5.1.3 Capital Programme

Affordability of capital expenditure plans is important in determining the overall robustness of the budget and adequacy of reserves to deal with potential variations.

The proposed Capital Programme for 2017 to 2020 of £48.6m is included within the report from the Executive Member for Resources. This predominantly comprises of existing commitments including investment:

- in our local transport plan
- in the highways network recovery programme and
- in aids and adaptations through provision of disabled facilities grants

Allocations are also included;

- for our successful Growth Deal 3 bid which will open up the Pennine gateways around the borough to facilitate housing and business growth
- to support continued investment in IT services to underpin our 'digital first' approach to delivering efficiencies and in turn, cash savings. Before projects are allocated funding from the reserve however, they will be subject to a rigorous business case approval process and detailed Member reports will be produced in line with financial procedures as required.
- to support the accommodation review which again will drive efficiencies and savings through rationalisation and a more cost effective use of space

These schemes will require strong project management and effective monitoring to ensure they are achieved on time and within budget. Failure to deliver against budget on such large schemes could lead to potential overspends which could impact on the overall future capital programme as additional costs could put pressure on the funding available for delivery of other schemes within the programme. To mitigate this risk, sound systems of internal control are in place with project boards established to provide the necessary governance structure, ensuring appropriate and timely reporting mechanisms.

5.1.4 In year financial Monitoring Process

The Council continuously seeks to strengthen its financial processes and controls. This approach, combined with existing effective arrangements, will provide a strong foundation enabling Members and Officers to continue to deliver the demanding targets and plans set within the Budget Strategy and the challenges identified for future years. In any budget however there are likely to be risks. In year financial monitoring processes are in place to mitigate these;

- Overall budget monitoring takes place throughout the year at both Portfolio and Executive Board level to identify potential areas of pressure and to develop and implement corrective action. This in itself provides a strong control environment and is commensurate with sound corporate governance. Progress against efficiency targets is also monitored and reported to Executive Members.
- The Chief Executive and Deputy Chief Executive meet at least once a month with the Director of Finance and IT, and senior finance staff, to review both the Councils' overall financial position and the progress made in delivering the savings programme, as well as considering the impact of emerging changes in the local government financial landscape
- The Policy & Corporate Resources Overview & Scrutiny Committee meets regularly with the Executive Member for Resources, and with the Director of Finance and IT and Director of HR, Legal and Corporate Services, to review the Council's budget position and progress made against the agreed savings programme.
- The Workforce Management Group, chaired by the Director of HR, Legal and Corporate Services, with senior finance and Trades Union representation, meets fortnightly and reports to the Deputy Chief Executive. The group oversees all workforce related restructuring and downsizing activity.
- The financial model that underpins the MTFS is subject to continuous review throughout the year to enhance forward planning, policy prioritisation, resource allocation and assess opportunities to invest in achieving future efficiency savings. The assumptions, variables and information within the model are regularly updated to ascertain the impact of known changes (e.g. legislative changes such as the National Living Wage), potential changes (such as adjustments to government funding and precept levels), and also for the refinement of variables (such as inflation, interest rates and employers pension rates) in light of emerging information.
- The Council adopts a risk based approach to financial management which provides added value to the governance process and identifies risks associated with both the revenue and capital programme. The provision of sufficient levels of Unallocated Reserves, and for specific contingencies within the budget, mitigates against the

financial risks from unforeseen financial issues so that these can be addressed in a responsive and controlled manner. As part of its approach to risk management the Council also makes provision for Earmarked Reserves, i.e. funding reserved to address specific future needs.

5.1.5 Risk

Ultimately the robustness of the budget is dependent on the strength of the arrangements in place to deliver the component parts and to manage the associated risks of each of these.

It must be recognised that given the significant reduction in resources, and the resulting reconfiguration of the organisation and its services, the Council faces significant risk which impact upon the financial estimates included in this budget.

These risks include:

- potential increase in demand for services from residents, particularly social care services for the most vulnerable, which may be exacerbated by reductions in public sector expenditure in other areas such as the NHS and as a result of Welfare Reform
- the reaction by residents to changes to services
- the ability to raise revenue from taxes, fees and charges
- changes in statutory and legislative requirements, including employment law
- changes by government in funding formula
- contractual obligations
- the challenging timescales in which to deliver the reductions
- potential loss of skilled and experienced staff
- the development of free schools and academies and further education reforms

The approaches outlined in this paper in relation to risk management, scrutiny, continuous monitoring of both the current and forecast financial position, as well as regular modelling through the MTFS of the financial impact of changes in the external environment, should mitigate these risks; by identifying the risks and providing an assessment of exposure, magnitude and potential financial impact, plans can be developed and implemented to address them. Therefore this Budget Strategy, whilst undoubtedly challenging, is achievable with strong project and risk management and with effective financial control.

5.2 Adequacy of Proposed Financial Reserves

Reserves are an essential part of good financial management; they help the Council to cope with unpredictable financial pressures, help to smooth the impact of known spending requirements over time and help to fund any in-year overspends. As funding levels have continued to reduce, local authorities have had to utilise reserves to cover any shortfalls in year to bridge the gap whilst cost and service reductions are fully implemented to address the imbalance; this has also been the case in Blackburn with Darwen.

There is no set formula for deciding what level of reserves is appropriate and every Council is free to determine the level they hold; holding a low level of reserves offers little resilience to financial shocks and sustained financial challenges however if

reserves are too high, there may be opportunity costs involved resulting in a lack of investment in services that could provide better outcomes for residents, and/or increased savings, and/or revenue generation for the Council.

As such the level, purpose and planned use of reserves are important factors to consider in developing the MTFs and annual budget.

5.2.1 Unallocated Reserve

A General or Unallocated Reserve has been established within the budget to provide a contingency to cushion the impact of unexpected events or emergencies and to meet potential liabilities, such as contingent liability claims.

The calculation to support the 2017/18 budget is detailed at **Appendix A**. This is based on a framework that has been developed to identify areas of risk, an estimate of their financial value and an assessed level of the risk coming to fruition. This process produces a value from which a risk assessed, minimum level of Unallocated Reserves can be determined. The calculation also allows for the current pressures on the Council's finances e.g. pressures in demand for social care services.

The sensitivity and risk analysis identifies a General Reserve requirement of £4.0m to provide financial resilience in the event of unexpected spending pressures.

5.2.2 Earmarked Reserves and Provisions

Earmarked Reserves are established to meet known or expected future liabilities where it is difficult to be specific about the exact financial amount of liability.

There are several categories of Earmarked reserves that the Council holds;

- Sums set aside for major schemes such as capital developments or to fund major reorganisations
- Insurance reserves
- Reserves retained for service department use
- School balances

The current forecast for Earmarked reserves at 31st March 2017 comprises;

£13.4m - total reserves of Council Use

£18.1m – Other reserves (including Schools)

During the course of 2017/18 it is anticipated that a net £1.6M will be transferred to Earmarked Reserves to fund known commitments. A full breakdown of the Earmarked Reserves is attached at **Appendix B**.

A review of the Earmarked Reserves held by the Council has also been undertaken to establish the purpose of the reserves and the likely timescale for their use.

6. LEGAL IMPLICATIONS

This report is a requirement under Section 25 of the Local Government Act 2003.

7. RESOURCE IMPLICATIONS

There are no resource implications as a direct consequence of this report

8. EQUALITY IMPLICATIONS

There are no equality implications as a direct consequence of this report

9. CONSULTATIONS

None applicable to this report

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Date:	27 th February 2017
Background Papers:	Budget Papers elsewhere on this agenda

GENERAL FUND UNALLOCATED RESERVES

General reserves are available to assist as working balances to help cushion the impact of uneven cash flows, and as a contingency against unexpected events or emergencies. They can also serve to provide short term funding in advance of funding allocations. The table below identifies a number of issues that pose risks against the budget. These figures have then been scaled back by a factor of 50% as it is unlikely that all these events would occur or indeed happen at the same time.

<u>Risk Event</u>	<u>£ 000's</u>
<p>General budget risks</p> <ul style="list-style-type: none"> • Demand pressures – significant parts of the Council's budget, particularly in Adults and Children's Social Care, are 'demand led' and can create significant demands for increased expenditure during the year • Overspend of budgets within service areas • National Living Wage – provisions made for increases in contracts for services, particularly in the care sector where many employees are currently paid at or close to the National Living Wage, will be insufficient to meet the increase in contract costs • Funding through the Revenue Support Grant will be insufficient to cover the additional costs of implementing the Care Act requirements • Inflation is underestimated or cannot be contained within existing budgets • Cost increases e.g. large scale increases in gas and electricity 	3,000
<p>Savings Programme</p> <p>The savings programme includes a number of saving proposals where implementation may be delayed or may not be achieved. Whilst the Council holds a Part Year Effect of Savings Reserve to mitigate the financial impact of such occurrence, and monitors and manages achievement of the programme through budget management at Director, Executive Member and Executive Board level, given the magnitude of the savings required, this remains a risk</p>	1,250
<p>Risk of reduced revenues from rents, fees and charges</p> <p>In addressing the reductions in funding, the Council has sought to maximise all available income streams to reduce the budget gap. Given the economic climate, and the risk that as schools convert to Academies they will not require support from the Council, income streams could be at risk.</p>	500
<p>Interest rates</p> <p>Although interest rates have been historically low for several years, the difficulties in the global economy expose the UK to potential, but unexpected, interest rate changes. As such there is a risk that in relation to borrowing, rates are understated and interest receivable estimates are overstated.</p>	100
<p>Emergencies</p> <p>The Council is required to maintain provision to meet the cost of emergencies that cannot be met from budgets or by insurance cover. Significant costs on emergencies are met by Central Government under the "Bellwin" scheme but these are only triggered once the Council's expenditure has exceeded a pre-determined limit (0.1% of the revenue budget). Only 85% of the costs above this limit are then covered.</p>	250

<u>Risk Event</u>	<u>£ 000's</u>
<p>Contingent liabilities</p> <p>The Council does not maintain a 'general' contingency within its revenue budget but relies on in-year savings and balances to meet any unexpected demands. Unexpected demands, particularly those that result from a legal decision, a change in government legislation or a determination in government legislation, could present a risk to the Council's finances.</p>	1,500
<p>Welfare Reform and Universal Credit</p> <p>The impact of the changes on the Council's financial position are difficult to predict and therefore as each of the reforms and changes are rolled out, there is a risk of increase in the net cost of housing benefits, an increase in the cost of council tax support and an increase in demand for services from those hardest hit financially</p>	500
<p>Litigation Claims</p> <p>As the Council faces reductions in resources for future provision of services there is an increased risk of litigation, albeit that robust risk assessment procedures and sufficient insurance policies are in place.</p>	400
<p>Risk of business rates shortfall</p> <p>The risk of a reduction in collection rates due to the recent revaluation, to both in terms of outstanding and potential future rating appeals and due to the economic climate.</p>	500
SUBTOTAL	8,000
Adjustment to reflect the unlikely probability that all of these events take place simultaneously (50% likelihood)	- 4,000
Recommended minimum level of Balances	4,000

	2017/18 £'000	2018/19 £'000	2019/20 £'000
Projected level of balances at start of each year	4974	4,974	4,974
Budget proposals – contributions from (-) or to (+) balances	0	0	0
Balances estimated at end of each year	4,974	4,974	4,974

EARMARKED RESERVES

The Council has a number of reserves which have been earmarked for specific purposes. These reserves are listed below, together with the purpose of the reserve and the amounts.

Name	Purpose	Balances estimated at 1 April 2017	Planned movements 2017/18	Balances estimated at 31 Mar 2018
		£ 000's	£ 000's	£ 000's
Reserves held for discretionary use by the Council				
Specific project reserves	Revenue savings that have been earmarked for specific projects or purposes in future years	6,726	350	7,076
Disabled Facility Grants	To meet increased demand for DFGs	289	0	289
Collection Fund Deficit	To meet any future Collection Fund Deficit whether Council Tax or Business Rates	268	0	268
Highways Winter Maintenance	This reserve has been built up from budget underspends on winter maintenance and supplementary allocations to provide additional maintenance requirements in the event of severe winter weather conditions	121	0	121
Support for Future Redundancy Costs	This reserve is to support future remodelling of services	2,713	623	3,336
Part Year Effect of Future Savings Plans	This reserve is to support the delivery of future budget reductions	1,640	700	2,340
Review of Services Provided Through the Strategic Partnership	This reserve is to support the reviews of services previously provided through the multi-disciplinary strategic partnership	304	0	304
Reserves held for specified (non-discretionary) purposes				
Maintenance of Wainwright Bridge	This reserve is the result of a contribution from Network Rail as maintenance of the new Wainwright Bridge becomes the responsibility of the Council – the reserve will support the portfolio once ongoing maintenance liabilities start to arise	506	0	506
Sc 106 income (under the 1990 Town and Country Planning Act)	Developers' contributions to be applied to enhance or maintain infrastructure and facilities	249	(100)	149
Highways Claims	This reserve is required to support anticipated future highway claims in respect of 2013/14 and earlier years	261	0	261
Contingent liabilities – MMI scheme of arrangement	Following the liquidation of Municipal Mutual Insurance (MMI) in 1992, the Council will be liable for a share of claim liabilities in the event of an insolvent run-off, which is increasingly more likely	250	0	250

Name	Purpose	Balances estimated at 1 April 2017	Planned movements 2017/18	Balances estimated at 31 Mar 2018
		£ 000's	£ 000's	£ 000's
Arts Acquisition Fund	This fund was established so that new pieces of art can be purchased as and when they become available	13	0	13
Winifred Ferrier Bequest	The money was bequeathed to the Council to enable the purchase and exhibiting of items associated with the life of Kathleen Ferrier	20	0	20
TOTAL RESERVES FOR COUNCIL USE		13,360	1,573	14,933
Reserves held in respect of joint arrangements and charitable bodies				
Darwen Market Traders	Funds held by the Council on behalf of Darwen Market Traders' Association	2	0	2
Joint Building Control Account	Accumulated surpluses in relation to the Joint Building Control agreement	145	0	145
Turton Tower Charity	Funds held by the Council in its role as trustee for the charity	36	0	36
Local Safeguarding Children's Board Fund	This fund was established from specific contributions to be used to support the LSCB	180	0	180
Reserves held in relation to schools				
Dedicated Schools Grant - surplus	DSG received but not yet deployed to meet expenditure properly included in the Schools Budget	9,455	0	9,455
LMS Schools balances	Funds held by schools under a scheme of delegation	*8,305	0	*8,305
TOTAL OTHER RESERVES		18,123	0	18,123

* use of reserves to be determined through the Schools' Forum