Robustness of Estimates and Adequacy of Reserves
(Incorporating the Reserves Policy)

Background

1) Since coming into being on 1 April 2009 Central Bedfordshire has made annual improvements to the corporate budget process. This has enabled a greater insight into trends over time as the amount of robust historical information continues to grows.

2) Past experience, combined with an assessment of future risks and opportunities, provides a sound basis for determining the robustness of estimates and appropriate levels of reserves for existing services.

3) However, the Budget for 2016/17 and current MTFP is set against a rapidly changing environment for local government. Consultation is currently underway on changes to the New Homes Bonus system and the Retained Business Rates (NNDR) system will also be subject to significant change over the MTFP period.

4) This means that there is a greater degree of financial uncertainty for the Council than has been the case for a number of years, and consequently a greater degree of estimation in the Budget and MTFP numbers. Whilst currently relatively well placed to accommodate these changes, the Council will nevertheless have to maintain adequate reserves to respond to unforeseen impacts.

5) This is demonstrated by the need to propose the use of £2.5M of reserves in 2016/17 in order to balance the budget following the Settlement Funding Allocation issued in December 2016. This unwelcome development is clearly not sustainable in the long term, but in mitigation, the MTFP sets out the intention to replenish Reserves over the course of the plan period.

Robustness of Estimates

Overall Approach

6) The 2016/17 Budget setting process formally commenced with the approval of the process and Budget Strategy at the Executive meeting on 4 August 2015. The Strategy assessed the assumptions in the existing Medium Term Financial Plan (MTFP), approved by Council in February 2015, in light of the continued challenging economic situation and the Government’s commitment to reduce overall public spending.

7) The 2016/17 Budget process was based on a refinement of the process undertaken for 2015/16. This included a series of reviews at Assistant Director (AD) level at an early stage during the process. These reviews involved each AD making a presentation to senior management which:

- provided an overview of the service;
- split the budget into activities and explained the basis for the total budget for each activity;
- identified pressures and efficiencies, both existing in the previous MTFP and new items and;
- outlined potential options for further savings;

8) As a result, the budget process allowed for full consideration of where savings could be made. Relevant Portfolio Holders were involved in each of the Directorate reviews to provide direction on political priorities.

9) The baseline position for the budget reviews was the 2015/16 agreed budget.

10) This process allowed for savings proposals to be developed across the late summer and early autumn. During January/February 2016 all Overview & Scrutiny committees reviewed the Draft Revenue Budget, including savings proposals and pressures, the Draft Capital Programme and the Draft Landlord Services Business Plan (Housing Revenue Account).

11) The latest position was presented to the Executive, together with the Draft Budget and the most up to date information on funding available at that time, on 12 January 2016. Public consultation commenced with the residents of Central Bedfordshire when the papers were published on 23 December 2015. Staff have also had the opportunity to input into the savings proposals as they have been assessed within Directorates.

12) The Chancellor of the Exchequer did not deliver the Autumn Statement until 25 November 2015 with the subsequent announcement of the Finance Settlement on 17 December 2015 (updated on the 23rd December 2015). Although in line with the timetable of last year, these late announcements meant there was little time in which to assess and incorporate changes to assumptions following the Settlement.

13) The Settlement figures for 2016/17 – 2019/20 were significantly worse than the Spending Review in November 2015 indicated it would be with very substantial reductions in funding. This has therefore resulted in a budget shortfall where additional savings will have to be identified in future years in order to present a balanced position. This is not new, as previous MTFPs have also not balanced over the medium term and it does not represent any immediate risk, but rather emphasises the need for further financial planning in the medium term. It also supports the requirement for holding reserves.

Budget Assumptions

14) The headline assumptions within the Budget cover the levels of funding received and inflationary pressures, as well as the consideration of Directorate pressures and efficiencies outlined above. All of this has been considered in the context of the national economic conditions, and those specifically relating to Central Bedfordshire.

Funding sources

15) The main funding sources are Revenue Support Grant (RSG), Retained Business Rates (NNDR), specific grants and Council Tax.

16) The Local Government Financial Settlement repeated the '4-block model' and used the floor damping methodology introduced for 2011/12, which groups authorities into four separate floor bands.

17) The Settlement has provided figures for the next four years with an offer to councils of a four year settlement should they wish to take advantage of that. Further details about the process to accept that offer are still awaited.

18) This will give some certainty over the medium term, but will only relate to the Revenue Support Grant which is due cease by 2019/20.

19) New Homes Bonus (NHB) amounts for future years of the MTFP are subject to consultation, and consultation on NNDR changes is expected to commence in summer 2016. These are likely to result in significant change.

20) This potential volatility adds uncertainty to financial estimates and makes long term planning more difficult. Appendix F to the budget report sets out the funding anticipated to be received from various sources, showing year on year movements to each source.

21) In line with currently announced intentions, Central Bedfordshire will continue to benefit significantly from the New Homes Bonus for the next two years. The grant is built into the overall resources in the Budget and is predicated on housing growth over the medium term. Clearly any slowing of growth is a risk to the Council's finances.

22) The Government has committed to reviewing the New Homes Bonus. In light of this uncertainty, the MTFP takes the prudent approach of capping the level of grant assumed to be received at the 2014/15 level (£6.95M). Where any additional amounts are received, these will be held in a reserve that will be used to fund infrastructure costs incurred as a result of growth and to mitigate budget pressures. From 2018/19 the amount of NHB received is expected to drop to c£7.0M as suggested in the Comparative Spending Methodology used as part of the Financial

Settlement. However, some of the options currently being consulted on could reduce this substantially.

23) Historically, CBC has frozen council tax, however, the Financial Settlement this year is predicated on an assumption by Government that all upper tier local authorities will increase council tax by 2% as an adult social care precept (ringfenced) and a further 1.75% general council tax increase to make up for the reduction to RSG. The budget consultation currently underway includes these proposals.

24) In addition, the Council Tax Freeze Grants from Central Government provided for previous years has now been rolled into the RSG baseline and so is lost as RSG is removed. The same treatment has been applied to the Care Act funding of £1.2M
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25) Central Bedfordshire has, since 2013/14, been able to keep a portion of National Non-Domestic Rates (NNDR) income under the Business Rates retention scheme. The MTFP takes a prudent approach to recognising NNDR growth over and above the Government's baseline estimate, based on modelling of planning data and anticipated business expansion.

26) The financial estimates are complicated by a series of grants received from Government to compensate for nationally imposed restrictions in the increase of NNDR to 2%, rather than following RPI as previously indicated. Prudent assumptions relating to the value of these grants in future years have been made.

27) The Council's plans for NNDR are ambitious and backed up by detailed working based on known development activity. However, the Business Rates Revaluation due in 2017 and also the NNDR consultation add significant risks to this funding source.

Inflation

28) The key assumptions are set out in the main body of the report and cover pay award, specific changes to pension arrangements and national insurance and non pay inflation.

29) The outlook for the economy is continuing to give rise to general pay restraint and for this reason a 1% increase only is provided for in the years of the plan beyond 2016/17. All pay awards are subject to national negotiations.

30) The Government has introduced a National Living Wage from April 2016 with the aim to achieve a minimum hourly rate of £9 by 2020. The rate for 2016/17 will be £7.20. This will put further pressure on Council costs.

31) Following the practice adopted the previous year, a general percentage uplift on non-pay items was not allocated for 2016/17. Instead, specific

inflation was provided only on a case-by-case basis where contractual conditions or similar factors necessitated an uplift. This ensures that inflation provisions are better targeted to the right areas.

32) The November 2015 Quarterly Inflation Report issued by the Bank of England advised that in September, twelve-month CPI inflation stood at -0.1%, slightly over 2 percentage points below the inflation target.

33) Around 80% of the deviation from the target reflects falls in energy, food and other imported goods prices, with the remainder reflecting subdued domestic cost growth. The combined weakness in domestic costs and imported goods prices is evident in subdued measures of core inflation, which are currently around 1%.

34) The Governor of the Bank of England also advised that inflation over the next few months could remain at current levels and that he did not expect inflation to reach the targeted rate of 2% for the next two years. The Bank also cut its prediction for UK economic growth in 2015 to 2.9%.

35) Interest rates remain very low, with the Bank of England base rate fixed at 0.5% since March 2009. It is not envisaged that this will change in the immediate future with the Bank of England signalling that rates will remain on hold until probably at least the second half of 2016 given the weakness of global growth and a low risk of inflation.

Service Expenditure

36) The robustness of estimates for each of the Directorates has been considered during the budget setting process, with an assessment of the general robustness of service budgets as well as the impact of pressures, growth and efficiencies.

37) The Base Budget build provides assurance that budget and activity are aligned and that budgets are at the correct level for 1 April 2016. A core part of the budget strategy has been to ensure that additional resources are allocated to those areas experiencing continuing pressures. These are detailed in the body of the report.

38) There is an Efficiencies Implementation Group in place, chaired by the Chief Finance Officer, which will oversee the delivery of all efficiencies; ensuring plans are in place to secure the required savings. This is a continuation of previous years' practice which has successfully overseen the delivery of significant savings. Nevertheless, continued delivery of further savings year on year, including £15.3M of savings in 2016/17, is a significant challenge.

39) This successful track record demonstrates a sound corporate approach to the delivery of budgeted savings and gives a measure of confidence that the 2016/17 Budget is realistic and achievable. Nevertheless each year it becomes harder to deliver savings whilst maintaining service

levels and there will be significant challenges to be faced in the years ahead. This is reflected in the fact that for the years 2017/18 onwards, the MTFP continues to shows that additional, as yet unspecified, savings will need to be delivered. Together with those savings that have been identified, these total £44.7M.

40) The Revenue budget for 2016/17 also includes a contingency of £2.1M which should help to mitigate any unforeseen pressures, or risks that might materialise.

41) Expected capital receipts exceeds the budgeted amount in order to allow for non achievement. If realised, these will also help to reduce the Council's need to borrow to fund the Capital Programme.

Risk Assessment

42) The above assessment of the robustness of estimates has identified a number of risks in the budget.

43) The Efficiencies Implementation Group chaired by the Chief Finance Officer, risk assesses all planned efficiencies using a Red/Amber/Green status at the beginning of each year and tracks their achievement throughout the year. In the event of any shortfall against and efficiency, a compensatory saving is sought.

44) Risks and opportunities are also tracked monthly as part of budget monitoring and migrating action taken where necessary.

General Fund Balances and Reserves Analysis

Background	
1.1	The Chief Finance Officer has a statutory duty under Section 25 of the Local Government Finance Act 2003 to comment annually on the adequacy of the Council's General Fund (GF) Reserves. This is reported as part of the annual budget papers to Executive and Full Council and the analysis within this document supports the Chief Finance Officer's opinion.
1.2	The purpose of General Fund reserves are to act as: • A working balance to help cushion the impact of volatility in net expenditure or income across financial years*. • To smooth the flow of funds e.g. when faced with funding cuts a GF Reserve enables the Council to draw down on reserves whilst a permanent efficiency saving is implemented. • A contingency to cushion the impact of unexpected events or emergencies; • A means of building up funds to meet known or predicted requirements. Funds can also be set aside in the form of specific earmarked reserves, which are accounted for separately but legally form part of the General Fund balance. * This ability of reserves to react to volatility in income or expenditure is different from the availability of physical cash. The Council can maintain low liquidity balances, as set out in its Treasury Management Strategy, as it has sufficient and immediate access to debt finance.
1.3	When considering whether the level of General Fund reserves is both adequate and necessary, the Chief Finance Officer considers the strategic, operational and financial risks facing the Council and balances this against utilising the maximum resources available to the Council to achieve its objectives and ensuring that current resources are used to the benefit of the current tax payer.
1.4	The Chartered Institute of Public Finance and Accountancy (CIPFA) released a Local Authority Accounting Panel (LAAP) Bulletin 99 (July 2014) outlining key areas to consider when assessing the adequacy of reserves including: • The robustness of the financial planning process (including treatment of inflation and interest rates, estimates of locally raised income and timing of capital receipts) • How the Council manages demand led service pressures • The treatment of planned savings / productivity gains • The financial risks inherent in any major capital project, outsourcing arrangements or significant new funding changes

	• The strength of the financial monitoring and reporting processes • Cash flow management and the need for short term borrowing • The availability of reserves, Government grants and other funds to deal with major contingencies • The general financial climate to which the Council is subject and its previous record in budget and financial management.
1.5	In November 2013 the Audit Commission stated that: *“Reserves are an essential part of councils’ strategic, financial and risk management. Councils hold reserves either as a contingency fund in the event of unforeseen circumstances, such as unexpected demand for services or a shortfall in income, or to smooth the impact of planned spending requirements over time, for example, setting aside funds for staff redundancies or to invest in large-scale capital projects. Our 2012 report on councils’ decision making on reserves encouraged councils to:* • *examine routinely how much they hold in reserves, and the purposes for which reserves are held; and* • *ensure their decisions on reserves are clearly explained to local taxpayers to promote accountability.”*
1.6	The analysis in Table 1 examines the Council’s balances against the criteria outlined in LAAP Bulletin 99 and is based on the Council’s procedures and structures. However, the assessment necessarily includes an element of subjectivity and, in acknowledgement of this, incorporates a range of possible balances. The calculated range for recommended general fund balances remains at £11.5m to £25m. The upper end of the range includes the maximum unallocated balances the Council could justify holding, and if balances were at this level, the Chief Finance Officer may recommend that plans were developed to use balances to enhance the Council’s expenditure plans in the current year.
1.7	The expected closing balance for 2015/16 is £15.2m which is 4% of gross income and within the recommended range. Additionally £31.6m has been set aside as General Fund earmarked reserves for specific identified purposes. Appropriate use of these reserves is included within the budget estimates presented, although in some cases the use may span more than one year. As an emergency measure these earmarked reserves could provide additional resilience, and therefore assist as a mitigation of risk to the Council.
1.8	Monitoring of both general and earmarked reserves takes place every month, to ensure these are correctly identified and are being used appropriately. The creation of new earmarked reserves, and transfers to and from reserves, are subject to approval by Executive as part of the final budget outturn position for the year. The reserves position is therefore transparent to all Members.

Table 1 Assessment of Required General Fund Reserve Balances

Area of Risk	Details	Minimum	Maximum
The general financial climate to which the Council is subject	Local Government will see sustained reductions in Central Government Funding beyond 2016/17. The Chancellor has stated the Government's aim of running a budget surplus over the next parliament. The Chancellor has committed to achieving this without increasing taxes and has indicated that ring-fencing of NHS and Schools Funding will continue. As part of the Financial Settlement for 2016/17 – 2019/20, councils have been made an offer of a four year settlement subject to certain conditions. Further details are awaited, but it is likely that this will only apply to the RSG element of the settlement. This is against a backdrop of early signs that the UK economy is recovering, with unemployment down to 5% and continuous period on period growth. The Bank of England has maintained Quantitative Easing at £375bn and low interest rates awaiting stronger signs of recovery, particularly with the wider European economy still facing difficulties. Locally, Central Bedfordshire Council has included identified Central Government funding reductions within its Medium Term Financial Plan (MTFP). Though more slowly than in previous years, Schools continue to convert to Academy status placing them outside the Council's control. Education Support Grant funding is provided to Councils on a per pupil basis and is reduced with every Academy conversion. The anticipated reduction is built into the MTFP. In addition, there are financial risks to the Council as a result of decision taken by schools to change their age range from a three tier system to a two tier system. This could result in the Council having to pick up significant redundancy costs and deficits from schools that close as a result.	£2M	£4M
The overall financial standing of the authority	From commencing with reserves of £5.1M on 31 March 2010, Central Bedfordshire Council has steadily increased reserves to £15.2M as at 31 March 2015, which is 4% of gross income. This reflects continuous improvement in the financial strength of the Council. Additionally the Council at 31 March 2015 had £31.6M in General Fund earmarked reserves set aside for specific purposes. A balanced budget has been set for 2016/17. However, to achieve this the Council has had to draw on £2.5m of Reserves. This is not sustainable	£0M	£1M

	in the long term but the intention is to replenish Reserves over the plan period.		
Estimates of level of locally raised income	In 2013/14 the administration of Council Tax Support Scheme was localised with a 10% reduction in funding and National Non-Domestic Rates (NNDR) moved to a retention system, where Councils keep an element of business rates raised. Retention of an element of Business Rates by Councils means the organisation would benefit from higher Rates income than expected, but also suffer the consequences if Business Rates income was to reduce. The Government has introduced a safety net payment to prevent excessive losses and a levy on gains and Central Bedfordshire Council would be funded for NNDR losses above £2.2M in a financial year and would have to pay 24% of their share of any gains above their baseline funding as a levy back to Central Government. The new NNDR retention system requires Councils to determine a provision for NNDR appeals in future years, where individuals may successfully challenge their NNDR rating. Councils have had to set this provision which directly affects NNDR income and necessarily involves an element of subjectivity. Both NNDR and Council Tax income forecasts are based on the estimation of property bandings and rateable properties by valuation professionals in each respective area. As noted about NNDR there is a risk that this could be impacted by both the NNDR consultation and the Rebasing of Rateable Value in 2017.	£1M	£3M
The treatment of planned efficiency savings/productivity gains	The Council has set a balanced budget for 2016/17 which includes £15.3M of efficiencies. A further £29.4M of efficiencies are required over the subsequent 3 years to achieve the Medium Term Financial Plan (MTFP). The Council has a successful track record of achieving efficiency savings. Efficiencies are monitored in the Council by the Efficiencies Implementation Group (EIG) chaired by the Chief Finance Officer.	£1M	£2M
The treatment of inflation and interest rates	Limited inflation has currently been included in the 2016/17 budget and price inflation has remained low with both RPI and CPI now significantly below 2% set by the Bank of England. However, there do remain specific risks in relation to contracts and fuel.	£2M	£3M

	Low interest rates have been in place for a number of years, with the Bank of England base rate at 0.5%, resulting in the Council receiving low returns on its investments, which has been factored into the budget. The General Fund at 31 March 2015 had external General Fund debt of £147.6M, 77% (£113.1M) of which is from the Public Works Loan Board (PWLB), a Central Government loan facility, 14% (£21M) was short-term fixed rate borrowing from other local authorities and 9% (£13.5M) was Market Debt from banks. Some £37.1M of the overall borrowing is based on either a variable rate of interest or reaches maturity within twelve months (temporary fixed rate debt). As at 31 March 2015 the Council had deferred accessing external debt to a value of £120M by borrowing from internal cash balances. An increase in interest rates would therefore have a direct and immediate cost on variable borrowing. Where amounts which have been internally borrowed are required to be spent, external borrowing may be required at that time to fund these and this would be at a cost to the organisation at that time depending on the rate of interest. The Council has a significant Capital Programme which forecasts £99M of borrowing over the next 4 years. At present the MTFP has calculated revenue implications on current interest rates and debt taken out on a short term basis. If interest rates were to increase, the revenue implications of this debt would increase when borrowing or refinancing the debt in future years.		
The financial risk inherent in any major outsourcing / insourcing arrangements	The Council has a number of high value contracts with external providers. The largest of these are contracts for: waste management, highways, passenger transport, social care for residential and nursing care provision, temporary accommodation, agency staff and grounds maintenance. Some of these suppliers are reliant on private finance linked to asset values for their viability. In the current financial climate this poses an increased risk of service failure to the Council. The Council has also engaged with a supplier to run its leisure centres, in a contract which creates a residual risk to be managed by the Council.	£1M	£2M
The treatment of demand led pressures	The Council faces significant population growth by 2021 with: • a 35% increase in the over 65's population;	£1M	£2M

	• a 44% increase in the over 85's population ; and • a 74% increase in the over 90's population. The Council has a robust Medium Term Financial Plan (MTFP) process embedded across the organisation. Through this process, reasonable assumptions about demand and funding pressures have been made and a prudent view of volatile areas has been taken. All known pressures across the Council are included as funded items in the MTFP, with additional funding in future years linked to forecast demand. The budget contingency is largely to take account of potential demand led pressures on key expenditure and income streams.		
The financial risks inherent in any major capital developments	The Capital Programme includes expenditure over the next 4 years of over £308M with substantial investment in schools places, enhanced waste disposal facilities and the Woodside Link. A further £36M of expenditure is on the capital reserve list, to be included in the main programme if the project can be accommodated within the Council's financing constraints. There is also expected to be significant investment through the Housing Revenue Account. Increased capital activity and development will result in a corresponding increase in financial risk.	£0.5M	£1.5M
Estimates of the level and timing of capital receipts	Capital Receipts are forecast to be £33.5M over the next four years, based on a schedule of land and properties that have been identified for disposal and form an important source of financing for the capital programme. If disposals are lower than projected then alternative options to achieve disposals or compensatory improvements to asset utilisation will be considered.	£2M	£3M
The availability of reserves, Government grants and other funds to deal with major contingencies and the adequacy of provisions	In the event of a major emergency it is possible that aside from general reserves, Central Government may provide funding to support the Council via the Belwin scheme. However Councils will only be able to access this funding if they have already spent 0.2% of their budget on repairs and thus may incur direct costs as a result.	£0M	£0.5M
The Council's capacity to manage in year budget pressures, and its strategy for managing both demand and service delivery in the longer term	There is a well-developed monthly budget monitoring process in place, ensuring adverse variations are identified promptly by service managers. The monthly challenge and review process ensures the early identification and resolution of issues. Additionally the 2016/17 budget includes a £2.1M contingency to potentially support any in year issues.	£0M	£1M

Miscellaneous	There are a number of risks that face the Council which have a low likelihood of occurring but would have a high impact if the risk was actualised. This includes risks of substantial flooding, disease outbreak or a serious service failure for example in Children's' Services or Adult Social Care. There is also the risk of widespread ICT failure. The Council has strong internal mechanisms for identifying, monitoring and reporting risks on a regular basis. Recent changes in legislation have brought about new community rights and alternative methods of delivering services traditionally provided by the Council. This has led to more and different supply chain partnerships being entered into, sharing risks across private, public and voluntary organisations. The Council may also face from time to time potential legal actions. Funds in excess of budgetary provision may be required to defend the Council against such actions.	£1M	£2M
Total		**£11.5M**	**£25M**