



Committee and date CMT 10 Jan 2010 Cabinet 19 January 2011	Item No Public
---	---

STATEMENT OF CHIEF FINANCIAL OFFICER ON THE ADEQUACY OF PROVISIONS AND RESERVES 2011-14

Responsible Officers Peter Timmins IHoF, James Walton S151

Email: peter.timmins@shropshire.gov.uk

Telephone: (01743) 252007

1. Executive Summary

- 1.1 Under Section 25 of the Local Government Act 2003, the Authority's Chief Financial Officer (Director of Finance) is required to report on the robustness of the estimates made for the purposes of the budget calculations and the adequacy of the proposed reserves. This report deals with the adequacy of the proposed reserves, which information enables a longer term view of the overall position to be taken, and seeks Members' approval for the recommended level of our reserves, based on an assessment of current financial risk.

2. Recommendations

- 2.1 That the Cabinet approve:
- A The recommended level of risk based general balances to support the 2011-14 revenue budget, be set at £13.342m;
- B The plan to reach this level of reserves over a longer period.
- 2.2 That the Cabinet note the projected recommended level for the following two years, £13.280m and £10.945m, respectively.

3. Background

- 3.1 There are two approaches for deciding the optimum level of the general Balances. Either a percentage of expenditure, which at one stage the Audit Commission set at 5% of revenue expenditure, or an approach based on a risk assessment of the budget, in the context of the Council's resourcing issues and pressures at the time.

This paper sets out the framework for a risk assessment approach. The issues that the framework considers include the following:

- The Council will need to budget for the cost of any redundancies necessary to achieve the required budget savings and service restructuring to the extent they are not contained in the budget proposals. The Council's policy is that redundancy costs are not contained in the budget proposals.
- There is always some degree of uncertainty over whether the full effects of any economy measures and/or service reductions will be achieved. Whilst the budget process has been prudent in these assumptions and that those assumptions

particularly about demand led budgets, should hold true in changing circumstances, an adequate level of general contingency provides extra reassurance the budget will be delivered on target.

- The Bellwin Scheme Emergency Financial Assistance to Local Authorities provides assistance in the event of an emergency. The local authority is able to claim assistance with the cost of dealing with an emergency over and above a threshold set by the Government (Shropshire's threshold for 2011-12 has been calculated at £759,000 which is approximately 0.2% of budget). The assistance is usually 85% of any eligible costs over the threshold. Any incident for which assistance is sought must involve conditions which are clearly exceptional by local standards and the damage to local authority infrastructure or communities must be exceptional in relation to normal experience. In the first instance these initial costs will have to be met from reserves.
- The risk of major litigation, both currently and in the future.
- Risk of changes to the levels of grant funding.
- The risk of losing subsidy arising from outstanding Housing Benefit and Council Tax Benefit Subsidy claims
- The risk of grants being introduced mid-year that require the Council to contribute.
- Unplanned volume increases in major demand led budgets, particularly in the context of high and accelerating growth.
- Changes in the economic climate which may influence certain levels of income to be received at a lower level than previous years, such as Planning fees.
- The need to retain a general contingency to provide for any unforeseen circumstances which may arise.
- The need to retain reserves for general day to day cash flow needs.

4. The Framework for the General Balance

4.1 The basis of the Framework is an area of risk, a budget amount, an assessed level of risk (high, medium, low), and a percentage factor, which will vary according to the level of risk which produces a value. The total of the value column is the level of balances required to cover the identified risk. The following example illustrates the text:

Salaries budget: £143m Risk: low Factor: 0.10% Value: £143k

4.2 The eleven areas of risk considered in the general contingency are set out in Appendix 1 with an explanation of the potential risks faced by the Council. Appendix 2 details the calculation of the General Reserves at £13.342m for 2011-12, £13.280m for 2012-13 and £10.945m for 2013-14.

5. Review of Earmarked Reserves and Provisions

5.1 To support the 2011-12 budget process a detailed review of earmarked reserves and provisions has been undertaken and has identified only one amount which can be released to support the General Fund :-

	£000
Waste Partnership General Reserve	1,400

5.2 This amount of £1.4m has been included for decision in the M8 2010-11 Revenue Monitor support the level of General Reserves recommended at 1st April 2011 and to underpin the 2011-12 budget.

6. General Fund Balance

6.1 It is essential in setting a balanced budget that the Council has money available in the event of unexpected spending pressures. The “balances” need to reflect spending experience and risks to which the Council is exposed.

6.2 Based upon the latest budget monitoring position at Month 8 it is envisaged that at the end of 2010-11 the balances will be £3.122m. This is significantly lower than the £11.7m risk based calculation of balances required for 2010/11. However, any additional funding sources or uncommitted expenditure identified between now and the year end is released to the General Fund Balance in order to reduce the gap. The budget strategy for 2011/12 also recognises that balances need to be increased and so has provided for a contribution to the General Fund Balance. However, it is not anticipated that this will fully close the gap in a single financial year.

6.3 The reduction in the calculated level of risk based balances needed in the following two years, reflects the reduced level of risk, particularly in the areas of “infant budgets” and “efficiency savings”. Therefore the risk of not holding a General Fund Balance at the required level is tempered by this reduction in future years.

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)
Human Rights Act Appraisal None.
Environmental Appraisal None.
Risk Management Appraisal The processes behind establishing the level of Reserves is well understood and seeks to mitigate the level of risk by adhering to its precepts.
Community / Consultations Appraisal None.
Cabinet Member Keith Barrow, Leader of the Council.
Local Member N/A.
Appendices Annex 1: Eleven Areas of risk for Shropshire Council Annex 2: Balances Calculation

Eleven Areas of risk for Shropshire Council

ANNEX 1

No	Area of risk	Explanation of risk
1	Inflation on expenditure	<p>There are two issues. Firstly, there may be some items of expenditure – fuel costs for example - where any estimate of inflation is a 'best guess'. The risk assessment puts a figure to the higher level of inflation that would seem to be unreasonable to include in a budget, but might come to pass.</p> <p>Secondly, information is less accurate for years 2 and 3; the risk assessment covers the higher range.</p> <p>At the present time the indications about inflation are a contradiction with reported reductions in some areas and increases in others. This makes it difficult to predict what will happen with the economy proving to be very challenging and looking forward there is uncertainty about what will happen and the level of inflation required.</p>
2	Interest rates on borrowing and investment	<p>This is similar to 1 above, but for a specific area.</p> <p>The expected impact of recent developments on interest rates on the 2011-12 budget will result in reduced interest earned on future money to be placed on the money markets. In the past it was possible for the Council to lend money and get a better interest rate than it was paying for borrowed money.</p> <p>The Council's borrowing has been undertaken at fixed rates of interest and so the level of interest payable is not considered as a risk to variable rates.</p>
3	Grants, Housing Benefits	<p>The Government system for allocating grants can appear short-term and a 'best guess' has to be offered in lieu of hard facts. Currently there are 2 issues:</p> <ul style="list-style-type: none"> • Housing Benefits – whilst the administration grant is straightforward (but reducing), the subsidy is subject to audit and, sometimes, abatement. The Council has no particular earmarked reserve to meet such an unforeseen cost should it occur. • On occasions general issues arise on grants which place the Council at risk of clawback.

No	Area of risk	Explanation of risk
4	Infant (estimated) budgets, (Inc or Exp) <ul style="list-style-type: none"> • Job Evaluation • Reorganisation incl redundancies • Transformation costs 	<p>There are some initiatives that are known will happen, but are not sufficiently advanced to accurately cost.</p> <p>The results on job evaluation scores but not pay have been passed to staff on 1st December 2008. Appeals on points are ongoing and it is unknown how this will impact on salary costs.</p> <p>As part of the budget process discussions have taken place with the DCLG re capitalisation of redundancies. A decision on whether this is possible is expected late in the budget process.</p> <p>The Council is currently going through a restructure process which it is anticipated may not be fully operational by the end of March to generate the savings it is planned to make.</p>
5	Volume changes - Demand led or volatile budgets (I or E) <ul style="list-style-type: none"> • Land sales • Collection Fund 	<p>Equally, there are long standing areas of risk, that are volatile – we budget for the middle of the range, but might find the actuality is at the higher end.</p> <p>In certain areas such as Land Sales the planned receipts estimated to the Council have fallen due to reducing market values and problems for potential procurers in obtaining finance. The effect of this has impacted on the Capital Plan.</p> <p>In respect of the Collection Fund then there would seem to be a risk that in the current economic downturn that the current projected levels of Council Tax collection fall leading to increased pressure on the Collection Fund.</p>
6	Efficiency savings	<p>The budget includes improvement programmes that will deliver savings; the risk is that they may be delivered at a slower rate.</p> <p>For future years there is a requirement on the Council to make year on year cashable efficiency savings.</p>
7	Insurance, funds and excesses	<p>Acts of God can result in higher insurance traffic than had been anticipated.</p> <p>Shropshire Council would seem to be well covered on this aspect re the general assessment of provisions and reserves in that it has based them on a detailed Actuarial Review given the potential impact of the economy which may lead to an increase in claims.</p>
8	Emergency planning – Bellwin, disaster recovery,	Were a disaster to occur, we must have a reserve in place to pick up costs that will fall to the Council.

No	Area of risk	Explanation of risk
	snow days	<p>The impact of flooding within the Council area based on present experience is that it is limited to localised pockets.</p> <p>The Council area has encountered budget pressures in the last two financial years due to extreme weather conditions and additional costs such as snow clearance particularly in winter.</p> <p>Other disasters such as those on ICT could occur on a one off basis.</p>
9	Changes (I or E) <ul style="list-style-type: none"> • Carbon Reduction Tax • LATS and Landfill costs • Debt Collection • Parking charges • Planning & Building Fees • Allowance for Budget Corrections 	<p>Change necessarily means doing things in a way for which we have no evidence. Our assumptions may be wrong. Also, the areas of change will alter over the years.</p> <p>This is the most difficult area to predict but there will be increased costs which are not foreseen when the budget is prepared. An example is developments on Shared Services and the timing of the beneficial impact on the Council.</p> <p>Other risk areas are seen to be increased costs on waste if recycling targets are not met; less income collected due to changing economic climate generally across the Council area; and a reduction in parking income as less people use retail facilities. An allowance for budget corrections has also been built in to accommodate any corrective action that needs to be taken if the assumptions about service delivery should change.</p>
10	Financial guarantees /legal exposure	<p>The contracts containing obligations that, if not fulfilled, would attract a penalty.</p> <p>The Council does have PFI Schemes. However there is no risk to the financing of the schemes at this present moment.</p>

Annex 2: Balances calculation

Balances Calculation											
2010/11			AREA OF RISK	2011/12			2012/13			2013	
Budget £000	Risk Level	Value £000		Budget £000	Risk Level	Value £000	Budget £000	Risk Level	Value £000	Budget £000	Risk Level
			Inflation								
143,125	0.10%	143.1	Salaries	125,607	0.25%	314.0	115,972	0.25%	289.9	114,929	0
14,352	1.00%	143.5	Premises	12,595	2.00%	251.9	11,629	2.00%	232.6	11,525	2
18,502	4.00%	740.1	Transport	16,237	4.00%	649.5	14,992	4.00%	599.7	14,857	4
55,225	1.00%	552.3	Supplies & Services	48,465	1.00%	484.7	44,748	1.00%	447.5	44,345	1
112,399	0.25%	281.0	Third Party Payments	98,641	0.25%	246.6	91,076	0.25%	227.7	90,256	0
75,017	0.25%	187.5	Transfer Payments	65,835	0.25%	164.6	60,785	0.25%	152.0	60,238	0
63,789	0.25%	159.5	Other	55,981	0.25%	140.0	51,687	0.25%	129.2	51,222	0
482,409		2,207		423,362		2,251	390,890		2,079	387,372	
			Interest Rates								
278,000	0.00%	0	Borrowing	278,000	0.00%	0	278,000	0.00%	0	278,000	0
99,932	0.20%	200	Investment	99,932	0.50%	500	99,932	0.50%	500	99,932	0
400	10.00%	40	PWLB	400	10.00%	40	400	15.00%	60	400	20
1,000	0.00%	0	Icelandic Bank exposure	220	10.00%	22	90	10.00%	9	90	10
		240				562			569		
			Grants								
81,000	0.25%	203	Housing Benefits	81,000	0.25%	203	81,000	0.25%	203	81,000	0
	Quantum		General Clawback		Quantum	0		Quantum	0		Quantum
		203				203			203		
			Infant Budgets								
1,500	1.50%	22.5	Job Evaluation	1,000	1.50%	15		1.00%	0		0
-	-	-	Reorganisation Savings	3,000	50.00%	1,500	3,000	50.00%	1,500	3,000	50
5,400	65.00%	3,510.0	Redundancy	2,700	20.00%	540	1,600	20.00%	320	800	20
250	10.00%	25.0	Transformation	1,400	10.00%	140	1,400	10.00%	140		
		3,558				2,195			1,960		
			Volume Changes								
28,900	1.00%	289.0	Land Sales	9,500	25.00%	2,375	10,000	25.00%	2,500	850	25
130,884	0.10%	130.9	Collection Fund	130,884	0.50%	654	130,884	0.40%	524	130,884	0
		420				3,029			3,024		
			Efficiency Savings								
2,000	50.00%	1,000	2010/11 Budget	-	-	-	-	-	-	-	-
3,074	0.25%	8	2010/11 Procurement	2,440	20.00%	488	2,334	10.00%	233	2,334	5
		1,008				488			233		
			Insurance								
3,945	0.00%	-	Provision	3,945	0.00%	-	3,945	0.00%	-	3,945	0.0
1,871	0.00%	-	Reserve	1,871	0.00%	-	1,871	0.00%	-	1,871	0.0
			Emergency Planning								
50	Quantum	50	ICT Disaster	50	Quantum	50	50	Quantum	50	50	Quantum
40	Quantum	40	Other Incident	40	Quantum	40	40	Quantum	40	40	Quantum
759	10.00%	76	Bellwin	759	10.00%	76	759	30.00%	228	759	50
1,469	70.00%	1,028	Severe Weather	1,469	70.00%	1,028	1,469	70.00%	1,028	1,469	70
		1,194				1,194			1,346		
			Changes								
-	-	-	Carbon reduction tax	-	-	-	900	50.00%	450	750	50
-	-	-	LATS Risk	522	10.00%	52	552	10.00%	55	1,690	10
3,902	-	-	Landfill Costs	3,741	7.50%	281	4,275	8.10%	346	4,809	10
15,603	0.10%	16	Debt Collection	15,603	1.00%	156	15,603	0.50%	78	15,603	0
3,150	10.00%	315	Parking Income	3,213	10.00%	321	3,277	10.00%	328	3,343	15
3,931	10.00%	393	Planning & Building Control fees	3,931	10.00%	393	3,931	10.00%	393	3,931	10
221,699	1.00%	2,217	Allowance for Budget corrections	221,699	1.00%	2,217	221,699	1.00%	2,217	221,699	1
		2,941				3,420			3,867		
			Financial Guarantees								
	Quantum		PFI (SWP)		Quantum	0		Quantum	0		Quantum
	Quantum		PFI (QICS)		Quantum	0		Quantum	0		Quantum
-	-	-	Street Lighting		Quantum	0		Quantum	0		Quantum
		0				0			0		
	Quantum		Other		Quantum	0		Quantum	0		Quantum
		11,769	TOTAL			13,342			13,280		