BALANCES AND RESERVES STATEMENT 2012/13

Contact Officer: Paul Whaymand
Telephone: 01895 566071

SUMMARY

The budget reported to Cabinet and Council in February 2012 contained an extract from the Balances and Reserves Statement 2012/13 which summarised the recommended range for unallocated balances. This Balances and Reserves Statement provides further detail on the Council's approach to the management and measurement of these, outlining technical accounting guidance used and analysis of specific risks that lead to a determination of a prudent reserves and balances range.

RECOMMENDATIONS

That the contents of the report are noted.

REASONS FOR OFFICER RECOMMENDATIONS

The balances and reserves statement has been produced based on an assessment of key risks and requirements for which balances and reserves need to be held by the Council, as part of exercising the Section 151 officer's professional duties with regard to budget setting.

INFORMATION

1 The Chief Finance Officer, as the Council's Section 151 officer has a legal duty to comment on the robustness of budget estimates for the forthcoming year including the adequacy of the Council's reserves as part of the statutory annual budget setting process. This duty stems from the financial governance framework established under the Local Government Act 2003.

2 For Hillingdon, this duty is exercised through an extract of the Budget Report to Cabinet and Council in February of each year. This statement expresses a prudent level of unallocated General Fund balances that the Council should hold as a range based on assessment of the key strategic, operational and financial risks faced by the Council.

3 In the 2012/13 budget report, the recommended range for unallocated General Fund balances to be set at £12m to £26.5m. The lower limit remains the same as that set for the last two years with the upper limit raised by £2.5m to reflect potential financial risk associated with medium term impact of Government proposals surrounding future financing streams for Local Authorities.

4 The attached Balances and Reserves Statement contains an underlying assessment against CIPFA criteria considering both internal and external financial risks to determine an identifiable recommended range for unallocated balances contained within the Budget Report.

LEGAL IMPLICATIONS

Decisions made by the Cabinet or a Cabinet Member must be 'Wednesbury' reasonable, i.e. Council officers need to present all the facts that are relevant to Members before they make a decision - otherwise decisions can be open to legal challenge.

BACKGROUND PAPERS

General Fund Revenue Budget and Capital Programme 2012/13 - report to Cabinet and Council February 2012

Local Authority Accounting Panel (LAAP) Bulletin 77 –Local Authority Reserves and Balances (November 2008)

STATEMENT ON 2012 ANNUAL REVIEW OF RESERVES

SUMMARY

The Council's Chief Finance Officer has a duty under the Local Government Act 2003 to comment on the robustness of the Council's budget for the coming year. This comment is also required to consider the adequacy of the Council's reserves and balances. The Chief Finance Officer has recommended that based on the 2012/13 budget an appropriate level of unallocated balances for the authority is in the range from £12m to £26.5m.

1. BACKGROUND

1.1 Under the Local Government Act 2003 the Chief Finance Officer has a duty to recommend to Cabinet the level of reserves and balances required by the Council. This requirement is met through the inclusion each year in the Budget Report to Cabinet and Council the results of a review of reserves and balances. This is done in line with current CIPFA guidance, which states that when reviewing the Medium Term Financial Forecast and budget the Council should consider the establishment and maintenance of reserves. These can be held for three main purposes:

- A working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this forms part of general reserves;
- A contingency to cushion the impact of unexpected events or emergencies – this also forms part of general reserves;
- A means of building up funds, often referred to as earmarked reserves, to meet known or predicted requirements – earmarked reserves are accounted for separately but remain legally part of the General Fund.

1.2 When assessing the appropriate level of reserves the Chief Finance Officer considers that the reserves are not only adequate but also necessary.

1.3 To do this, the strategic, operational and financial risks facing the Council are taken into account. The Council should retain adequate reserves to cover unexpected expenditure, allow contingency against implementation of major funding cuts and to cushion the potential impact of proposed changes to funding regimes. Equally the Council should seek to utilise the maximum resources available to achieve its objectives and to ensure that current resources are used for the benefit of the current tax payer. CIPFA do not recommend a stated amount or percentage of budget to be set as a reserve level recognising the many factors involved when considering an appropriate range can only be assessed locally.

1.4 Over the years, the Council has improved its level of reserves to an appropriate level from a relatively low base. However it still has a fairly low level of total reserves due to the relatively limited number and value of earmarked reserves compared with many councils.

1.5 Each earmarked reserve is subject to its own review of adequacy and a listing of these are detailed within the Statement of Accounts.

2. ADEQUATE LEVEL OF UNALLOCATED GENERAL FUND RESERVES

2.1 To determine the recommended level of reserves the Council has assessed risks it currently faces. Criteria as specified in Local Authority Accounting Panel (LAAP) Bulletin 77 (November 2008) have been followed for this purpose, alongside more recently indentified financial risks arising in the medium term as a result of government proposals. Details of which are shown in Appendix 1 and include:

- The robustness of the financial planning process (including treatment of inflation and interest rates and timing of capital receipts)
- How the Council manages demand led service pressures
- The treatment of planned savings / productivity gains and implementation of the Council's BID programme
- 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 to and its previous record in budget and financial management.

2.2 The assessment, although based on the Council's procedures and structures, does necessarily have an element of subjectivity. In acknowledging this, the optimum level of reserves incorporates a range. The recommended range for 2012/13 is £12m to £26.5m. The upper end of this range represents the highest level of unallocated balances that the Council could reasonably justify holding. If balances were above the upper level, the Chief Finance Officer would recommend that plans were developed to use the excess balances towards enhancing the delivery of the Council's strategic objectives in the current year. The equivalent figures recommended at the time of budget setting for 2011/12 were £12m to £24m.

2.3 The array of risk factors that determine the need to hold balances and reserves has changed since last year's budget setting process to include the forthcoming changes to local government finance, which include the ability to retain growth in Business Rates and the localisation of support for Council Tax, both changes effective from 1 April 2013. As a result of the review of these risk factors the assessment of the maximum level of balances has increased. Appendix 1 shows the adjustments in the level of General Fund reserves from 2011/12 to 2012/13, analysed across the criteria detailed above. The principle determining factor for the change is the general financial climate and the need to hold balances to manage the impact of significantly reduced Government grants and forthcoming legislative changes.

2.4 In summary, there is a broad spread of balances held against the key issues listed in paragraph 2.1. Therefore most of the Council's balances are held to deal with the common risks that most local authorities need to manage on an ongoing basis. However there are a number of key issues for Hillingdon that drive the need to hold additional balances. Firstly, the unique circumstances surrounding the presence of Heathrow Airport within the boundaries of the Council. In particular this is the driver of the Council's exceptional asylum caseload, which has a fragile, unpredictable and inadequate funding stream attached to the support for care leavers. Secondly, along with all other local authorities, the Council is implementing a significant transformation programme following the reduction to its funding as a result of the Comprehensive Spending Review announced in October 2010. As a result, savings of £26.2m were required in 2011/12 and the budget for 2012/13 contains savings proposals of £17.7m. Total savings as a result of the Spending Review will amount to £69.1m over this period.

2.5 In addition to these, over the medium term there are significant uncertainties in relation to both the funding of local Government and new burdens which may become the responsibility of local Government which make forecasting beyond 2012/13 difficult.

2.6 The most significant issues are in relation to the review of local Government funding. Following several consultations during 2011, the government announced in the Local Government Finance Bill that it will enable councils to retain a portion of the business rates generated locally to replace formula grant and that it would also localise support to council tax.

2.7 Retention of business rates would commence from April 2013, to align with the next two year local government finance settlement. Whilst it is too early to calculate the impact of the proposals, as much of the detail of the system has yet to be announced, initial analysis has highlighted a few key issues which could have a significant impact on the council's future funding. The most significant are that there will be no growth in the first 2 years, future growth will only be possible between resets (every 10 years) which will make long term planning difficult and the tariff (and top-up) will be uprated by RPI each year, which could be a disincentive to growth.

2.8 A further major issue relates to the reform of the benefits regime. Whilst Housing Benefit will be absorbed into the new universal benefit, Council Tax Benefit (CTB) will be abolished and replaced with a local support scheme with effect from April 2013. Each council will have to design, administer and run a local scheme, and do so with an immediate 10 per cent reduction in funding. The scheme will be funded through a specific grant from central government. Certain groups (such as pensioners) will be protected from any reduction in the level of benefits. The initial estimate of the funding shortfall to Hillingdon is £2.21m.

2.9 In addition, on 15 July 2011 the Department of Health confirmed the intention to transfer Public Health services from PCT's to local government with the intention of providing a service which focus on the prevention of illness. A ring fenced grant will be transferred from the NHS in April 2013, with shadow budget allocations due to be published shortly. Currently Hillingdon PCT has around £20m in resources to support public health activity.

2.10 Consideration of these risk factors have resulted in the upper end of the recommended range of reserves to be increased from £24m to £26.5m representing just 3% of gross expenditure and 6% of controllable expenditure if Schools budget and Housing Revenue Account are excluded.

2.11 The budget for 2012/13 includes a payment into balances of £2.2m. Balances are forecast to be at £21.3m as at 31st March 2012 and up to £23.5m at 31st March 2013. This should provide some contingency to help absorb any further adverse movement in central Government funding in addition to providing scope for absorbing any potential delays in the timing of the delivery of savings.

2.5 The General Fund revenue budget proposals for 2012/13 also include a contingency of £16.7m which is identified against specific risks that are funded within the budget. Many of these risks, although not precisely quantifiable, have a high degree of certainty that they will be called upon in the year.

3. EARMARKED RESERVES

3.1 The Council has ring fenced earmarked reserves with balances as at 31 March 2011 detail in table 2 below.

Table 2: Earmarked Reserves

Reserve	Balance as at 31 March 2011
Housing Revenue Account	£12.9m
Schools Delegated Funds	£20.2m
Schools Earmarked Reserves	£0.1m
Parking Reserve Account	£0.8m
New Roads and Street works Act	£0.2m
Insurance Reserve	£0.5m
Leisure Facilities Reserve	£0.4m
Housing Grant Funded Reserves	£0.4m
HRA Grant Funded Reserves	£0.1m
Libraries Reserve	£0.1m
Highways Reactive Maintenance	£0.5m
Social Care Grant Funded Reserves	£1.1m
Children Services Reserves	£0.3m

Total	**£37.6m**

3.2 Movement in and out of Earmarked reserves is generally determined on out-turn however it is expected that these will reduce by approximately £5m due to the withdrawal of schools reserves on becoming academies.

3.3 An explanation as to the function and source of funds for these reserves can be found in note 2 of the Statement of Accounts.

4. UNFUNDED RESERVES

4.1 Local authorities also hold other reserves that arise out of the interaction of legislation and proper accounting practice. These reserves, which are not resource-backed and can not be used for any other purpose, are also detailed in the Council's Statement of Accounts.

Risk Management

5.1 The Code of Audit Practice makes it clear that it is the responsibility of the audited body to identify and address its operational and financial risks, and to develop and implement proper arrangements to manage them, including adequate and effective systems of internal control. The financial risks need to be assessed in the context of the Council's overall approach to risk management.

5.2 The process by which the contingency budget is constructed links directly into the Council's risk management process. Significant risks are identified and recorded in risk registers which are regularly reviewed and updated as part of the risk management process. The process provides for review by senior officers, Group Directors, Cabinet Members and the Audit Committee addressing both executive functions and governance requirements. This process is integral to ensuring the effectiveness of the budget strategy. The key financial risks identified in the corporate risk register are reflected either directly in the budget strategy or are covered by the retained level of unallocated balances and reserves.

APPENDIX 1

Further detail on Assessment of Required General Fund Revenue Balances

Area of Risk	Details	Risk	Reserves Required 2012/13 (£m)	Reserves Required 2011/12 (£m)
The general financial climate to which the Council is subject	There remains an ongoing uncertainty in future funding arrangements for the council exacerbated by the wave of new initiatives and burdens.	Funding for 2012/13 is fairly certain, but there remains a risk of in year adjustments	1.5 – 4.0	2.0 – 4.0
The overall financial standing of the authority	The financial strength of the council continues to improve with strengthened treasury management, a smaller capital programme, a prudent projected increase in council tax base and adequate bad debt provision. Financing costs are well managed through effective borrowing strategies and provided for in the MTFF	Slightly higher balances are forecast at the end of 2011/12, although the contingency included in the 2012/13 budget has also increased to £16.7m	1.5 – 4.0	1.5 – 4.0
The treatment of planned efficiency savings / productivity gains	The budget for 2012/13 contains £17.7m of new savings, as a result of the front loading of the cuts in the CSR 2010. This comes on top of £26.2m of savings delivered in 2011/12. New savings proposals have been developed through the council's transformation programme and strong project management and monitoring arrangements have been put in place.	Governance arrangements have been strengthened, but there remains an increasing risk on the delivery of savings due to increasing volume being managed by a reducing workforce.	2.5 – 5.0	2.5 – 5.0
The treatment of inflation and interest rates	Limited inflation has been included in the 2012/13 budget and the current trend is decreasing. However, specific risks remain in relation to contracts and fuel. The low interest rate environment continues and this has been factored into the budget.	Despite the level of inflation decreasing, specific risks in relation to contracts and fuel remain.	1.0 – 2.0	1.0 – 2.0

The financial risk inherent in any significant new funding partnerships or major outsourcing arrangements	The Council is reliant on external providers for a range of key services, especially in social care for residential and nursing care provision, and housing providers for temporary accommodation. 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 outsourced facilities management, leisure management and revenues services, and these contracts create residual risks to be managed by the Council.	The risks around these arrangements, although well managed, are not fully mitigated and it is proposed that £1.0m is required to cover these.	1.0 – 3.0	1.0 – 2.0
The treatment of demand led pressures	The Council has a robust financial planning process (MTFF) 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 MTFF, 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.	This risk area is being managed through the MTFF and by including a £16.7m contingency within the budget. Even taking this into account it is prudent to have additional cover of £1.0m in reserves in order to mitigate the uncertainty over these pressures.	1.0 – 3.0	1.0 – 2.0
The financial risks inherent in any major capital developments	The Capital Programme contains fewer large projects than in recent years, but continues to include a significant volume of programme of works projects. However, a large part of the social care reablement programme is dependent on supported housing development which if slipped could impact on revenue savings.	£1.0m is proposed to be held in reserves to cover the impact of this risk.	1.0 – 1.5	1.0

Estimates of the level and timing of capital receipts	The estimate of the capital receipts in the 2012/13 - 2014/15 Capital Programme is based on a schedule of assets that have been identified for sale. If disposals are lower than projected then alternative options to achieve disposals or compensatory improvements to asset utilisation will be considered. The Council in addition has flexibility to borrow or use accumulated cash balances to cover such timing differences. The capital programme assumes General Fund capital receipts of £13.3m in 2012/13 and £12.7m over the following two years.	Risk has been minimised by only including receipts from identified surplus sites. However, the timing of receipts can have a significant impact on financing arrangements especially Minimum Revenue Provision (MRP) (typically 4% of the historic net capital financing requirement).	1.0	1.0
The availability of reserves, Government grants and other funds to deal with major contingencies and the adequacy of provisions	Whilst there remains a slight risk, the level of reserves has increased and an adequate level of provisions has been built into the budget.		0.5 – 1.0	0.0 – 1.0
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. In the longer term, the Council's transformation programme is addressing service delivery.	Although risk has been reduced by robust monitoring procedures an amount for this area is still included.	1.0 – 2.0	1.0 – 2.0