BALANCES AND RESERVES STATEMENT 2014/15

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SUMMARY

The budget reported to Cabinet and Council in February 2014 contained an extract from the Balances and Reserves Statement 2014/15 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 Corporate Director of Finance, 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 The recommended range for unallocated balances remains consistent with 2013/14 at £15m to £30m, with the overall upper limit for balances increasing by £5m to take account of the planning drawdown from reserves included in the Medium Term Financial Forecast for 2015/16.

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

The Council's Budget: General Fund Revenue Budget, Housing Revenue Account Budget and Capital Programme 2014/15 - report to Cabinet and Council February 2014

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

STATEMENT ON 2014 ANNUAL REVIEW OF RESERVES

SUMMARY

The Council's Corporate Director of Finance 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 Corporate Director of Finance has recommended that based on the 2014/15 budget an appropriate level of unallocated balances for the authority is in the range from £20m to £35m.

1. BACKGROUND

1.1 Under the Local Government Act 2003 the Corporate Director of Finance 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 Corporate Director of Finance 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.

1.5 Each earmarked reserve is subject to its own review of adequacy and a listing of these is 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 the 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 specific government proposals and transfer of new responsibilities to the Council. Details of which are shown in Appendix 1 and include:

- 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 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 and the adequacy of provisions;
- The general financial climate to which the Council is subject 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 2014/15 is £20m to £35m. 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 Corporate Director of Finance would recommend that plans were developed to use the excess balances towards enhancing the delivery of the Council's strategic objectives. The equivalent figures recommended at the time of budget setting for 2013/14 were £15m to £30m.

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 take account of the ongoing Governments reduction programme which will place greater pressure on the Council's Finances with cuts of 8% per annum expected in core funding in the medium term to 2018/19. Delivering this level of expenditure reduction year on year will need careful planning and longer lead in times to agree and deliver savings programmes across services. To manage the reductions in 2015/16 a planned drawdown from reserves is included for 2014/15 to support the budget in the following financial year. Appendix 1 summarises movements in the level of balances recommended to manage the criteria set out above.

2.4 In summary, there is a broad spread of balances held against the key issues listed in paragraph 2.1. 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.

2.5 Hillingdon has seen substantial population growth, evidenced by the 2011 census, which is set to continue into a period of further central government funding cuts over the medium term. Continuing pressures arising from demographic growth will see increased demand for key services, including Adult Social Care, Education, Housing and Waste Collection and Disposal. Secondly, a number of issues arise from the presence of Heathrow Airport within the borough. 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 asylum seekers.

2.6 In addition to these local issues, the 2012 Local Government Finance Act has resulted in a significant transfer of risks from Central Government in relation to both the localisation of Business Rates Income and introduction of a local Council Tax Reduction (CTR) Scheme. Whilst the first year of operating these significant funding changes in 2013/14 has not led to a draw on reserves, continued government tinkering with the amount of business rates income through restricting the increase in smaller business rates to less than inflation and the need to review the Councils CTR scheme for 2015/16 based upon the first years operation lead to continuing risks to the level of locally raised income.

2.7 Consideration of these risk factors have resulted in the level of unallocated reserves increasing at the upper level to £35m including a £5m drawdown planned for 2015/16 to support the budget in that year as set out above. This represents 7% of gross budget and 12% of controllable expenditure if Schools and Housing are excluded.

2.8 The approved budget for 2014/15 maintains balances at 2013/14 outturn levels, with neither a draw down from or payment into balances. The latest forecast for balances at 31 March 2014 as at period 9, is £36m

2.9 The General Fund revenue budget proposals for 2014/15 also included a contingency of £24.7m which is identified against specific in year 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 2013, which are divided between those held in statutory funds and those held for management purposes. Table 2 details the balances held at 31 March 2013.

Table 2: Earmarked Reserves

Reserves	**Balance as at 31 March 2013 £000's**
Housing Revenue Account Reserves	19,804
Schools Delegated funds Reserves	14,950
Statutory Funds Reserves	**34,153**
Abbotsfield School	94
Backdated Council Tax benefit	180
Capital Investment Pump priming	1,000
Children Services Reserves	205
Elections	280
Environmental Waste	470
Grant Funded Reserve	2,188
Highways management	909
Housing	830
HS2 Contingency	129
Insurance Provision	1,220
Leisure Facilities Reserve	11
Libraries Reserve	81
Miscellaneous	1,947
Music Bursary Fund	350
Wards Budget Initiative	125
Workforce Restructure	400
Management Reserves	**10,419**
Total	**45,173**

3.2 Movement in and out of Earmarked reserves is generally determined on out-turn however it is expected that Schools Delegated Funds will decrease 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 cannot 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	Reserves Required 2014/15 (£m)	Reserves Required 2013/14 (£m)
The general financial climate to which the Council is subject	Indications are that the sustained reductions in funding over the medium term with the reductions in spend in the public sector are likely to continue for the next few years.	1.5 - 4.0	1.5 – 4.0
The overall financial standing of the authority	The financial strength of the council continues to improve with prudent assumptions factored into the MTFF for growth in income, while a comprehensive development and risk contingency is funded for 2014/15.	1.5 – 2.0	1.5 – 2.0
Estimates of level of locally raised income	With the local retention of business rate revenues together with Council Tax and other income streams now amount to 70% of the council's corporate funding. There continues to be a risk from volatility in this income which would impact upon the Council's finances.	2.0 – 3.5	2.0 - 3.5
The treatment of planned efficiency savings / productivity gains	The budget for 2014/15 contains £12.8m of savings. Whilst governance and monitoring arrangements have been strengthened, with regular reporting on delivery of savings to Cabinet, delivering these savings on top of the £70m already delivered since 2010 becomes more difficult and therefore the risk of slippage or non delivery increases.	2.0 – 4.0	2.0 – 3.0
The treatment of inflation and interest rates	Limited inflation has been included in the 2014/15 budget to reflect the latest intelligence. However, specific risks remain in relation to contracts energy and fuel. The low interest rate environment is likely to continue in 2014/15 and this has been factored into the budget.	1.0 – 2.0	1.0 – 2.0
The financial risk inherent in any 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	1.0 – 2.0	1.0 – 3.0

	service failure to the Council. Although the Council has outsourced facilities management, and revenues services, some services have been in sourced including leisure management. These contracts continue create residual risks to be managed by the Council.		
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 demand led pressures 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 budgeted contingency and development fund is largely to take account of potential demand led pressures on key expenditure and income streams. The reduction in the level of required reserves for 2014/15 results from a lowering of the risk around the Council Tax Reduction scheme.	2.0 – 4.0	2.0 – 5.0
The financial risks inherent in any major capital developments	The Capital Programme includes substantial investment in primary and secondary schools and for new facilities such as a theatre and museum, which alongside the potential for extensive investment within the Housing Revenue Account will result in a corresponding increase in the level of financial risk arising from this significant investment.	1.0 – 3.5	1.0 – 2.5
Estimates of the level and timing of capital receipts	The estimate of the capital receipts in the 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.	1.0 – 2.0	1.0 - 2.0
The availability of reserves, Government grants and other funds to deal with major contingencies and the adequacy of provisions	Whilst there remains a continuous risk, the level of reserves has increased and an adequate level of provisions has been built into the budget.	2.0 - 3.0	2.0 - 3.0

Planned drawdown from balances in 2015/16	To manage the impact of funding further reductions of 8% in the council's budget in 2015/16 a drawdown from reserves is planned	5.0	N/A