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BALANCES AND RESERVES STATEMENT 2016/17

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SUMMARY

The budget reported to Cabinet and Council in February 2016 contained an extract from the Balances and Reserves Statement 2016/17 which summarised the recommended range for unallocated balances. The attached 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.

RECOMMENDATION

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 has been increased from £15m to £30m in 2015/16 to £15m to £31m in 2016/17, with the overall upper limit for balances £14m higher, at £45m, to take account of the planning drawdown from reserves included in the Medium Term Financial Forecast from 2016/17.
- 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.

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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: Medium Term Financial Forecast 2016/17 - 2020/21 - report to Cabinet and Council February 2016

Local Authority Accounting Panel (LAAP) Bulletin 99 – Local Authority Reserves and Balances (July 2014)

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STATEMENT ON 2016/17 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 2016/17 budget an appropriate level of unallocated balances for the authority is in the range from £15m to £31m. In addition to these unallocated balances, further sums in the range from £4.5m to £14m are recommended to manage the impact of continued severe funding reductions.

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 (MTFF) 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 category of earmarked reserve is subject to its own review of adequacy and each of these is detailed within the Statement of Accounts.

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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 99 (July 2014) have been followed for this purpose, alongside more recently identified financial risks arising in the medium term as a result of specific government proposals and transfer of new responsibilities to the Council. Details of these 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 Most of the Council's balances are held to deal with the common risks outlined above 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.

2.3 Hillingdon has seen substantial and sustained population growth, evidenced by the latest population estimates, 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 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.

2.4 In addition to these local issues, the 2012 Local Government Finance Act resulted in a significant transfer of risks from Central Government in relation to both the partial localisation of Business Rates Income and introduction of a local Council Tax Reduction (CTR) Scheme. No further transfers are planned for 2016/17, although the Government has stated their intention to increase the local share of Business Rates Income to 100% over the next four years. While such localisation is expected to provide a mechanism for the Council to benefit from local economic growth, the corresponding transfer of risk will continue to be reflected in the recommended level of balances.

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- 2.5 The array of risk factors that determine the need to hold balances and reserves have been reviewed since last year's budget setting process and the level of cover against each risk criteria refreshed, this has resulted in an increase in the maximum level of reserves by £1m to £31m in 2016/17. This additional provision has been made in respect of financial risk associated with externally contracted service provision, in particular reflecting the well publicised pressures on the social care sector.
- 2.6 The recommended range for unallocated balances is therefore £15m to £31m, an increase from the £15m to £30m range for 2015/16. The upper end of this range represents the highest level of unallocated balances that the Council could reasonably justify holding. As balances are above the upper level, the Corporate Director of Finance has recommended the use the excess balances in the Council's broader financial planning.
- 2.7 These excess balances will be required to support the Council's MTFE by smoothing the impact of substantial funding government funding cuts over the remainder of this parliament. A further £4.5m to £14m is included in the overall level of appropriate balances to support this strategy. Appendix 1 summarises the level of balances recommended to manage the criteria set out above, with the headline range for General Balances during 2016/17 being £19.5m to £45m.
- 2.8 The approved budget for 2016/17 includes a drawdown of £4.2m from balances, which are projected to reach approximately £37m by 31 March 2016 and therefore would result in excess of £32.8m by 31 March 2017. For the purposes of establishing a minimum level of balances, this drawdown has been rounded up to £4.5m.
- 2.9 The General Fund revenue budget proposals for 2016/17 also included a contingency of £18.4m 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 2015 Which are set out in the table below:

| Reserves | Balance as at 31 March 2015 £000's |
|---|---|
| General Fund Reserves | |
| Earmarked Reserves | |
| - Grants Unapplied | 6,005 |
| - Member Initiatives | 11,135 |
| - Other Reserves | 7,068 |
| - Public Health Reserve | 2,453 |
| - Parking Revenue Account / New Roads & Street Works Act | 633 |

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|------------------------------------|---------------|
| - PFI | 485 |
| Total General Fund Reserves | 27,779 |
| Schools Delegated funds Reserves | 16,606 |
| Total Reserves | 44,385 |

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.

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.

Assessment of General Fund Reserves Requirement

Appendix 1

| Assessment of General Fund Reserves Requirement | Minimum Level 2016/17 (£ million) | Maximum Level 2016/17 (£ million) | Minimum Level 2015/16 (£ million) | Maximum Level 2015/16 (£ million) | Principal Reasons for Requirement |
|---|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|--|
| The general financial climate to which the Council is subject | 1.5 | 4.5 | 1.5 | 4.5 | Sustained reductions funding forecast over the medium-term with the austerity agenda set to continue over this parliament |
| The overall financial standing of the authority | 1.0 | 2.0 | 1.5 | 2.0 | To manage adverse movement in the Council's financial standing |
| Estimates of level of locally raised income | 2.0 | 4.0 | 2.0 | 4.0 | Locally raised income accounts for approximately 70% of corporate funding |
| The treatment of planned efficiency savings / productivity gains | 2.0 | 4.0 | 2.0 | 4.0 | To manage risk around slippage of the Council's major savings programme, in response to funding reductions |
| The treatment of inflation and interest rates | 1.0 | 1.0 | 1.0 | 1.0 | With limited exposure to changes in interest and inflation rates, MTFF assumptions have been refreshed to reflect latest intelligence. |
| The financial risk inherent in major contract arrangements | 1.5 | 3.0 | 1.0 | 2.0 | To manage any impact of services arising from supplier risk, particularly in respect of Social Care provision |
| The treatment of demand led pressures | 2.0 | 4.0 | 2.0 | 4.0 | Increased demand for services from an aging and increasing population |
| The financial risks inherent in any major capital developments | 1.0 | 3.5 | 1.0 | 3.5 | Inherent risks due to significant level of investment required for school places |
| Estimates of the level and timing of capital receipts | 1.0 | 2.0 | 1.0 | 2.0 | Slippage on asset disposal programme could lead to increased borrowing |
| The availability of reserves and other funds to deal with major contingencies and pressures | 2.0 | 3.0 | 2.0 | 3.0 | Cover for unforeseen events over and above £500k budgeted provision for General Contingency |
| Unallocated GF Reserves | 15.0 | 31.0 | 15.0 | 30.0 | |
| Planned drawdown from | 4.5 | 14.0 | 5.0 | 15.0 | To smooth the front-loading of funding |

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Assessment of General Fund Reserves Requirement**Appendix 1**

| Assessment of General Fund Reserves Requirement | Minimum Level 2016/17 (£ million) | Maximum Level 2016/17 (£ million) | Minimum Level 2015/16 (£ million) | Maximum Level 2015/16 (£ million) | Principal Reasons for Requirement |
|--|--|--|--|--|--|
| balances 2016/17 | | | | | reductions, a planned drawdown from reserves has been included in MTFE |
| Total GF Reserves | 19.5 | 45.0 | 20.0 | 45.0 | |

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