South Oxfordshire District Council

Report of the chief financial officer on the robustness of the budget estimates and the adequacy of the reserves.

1. Section 25 of the Local Government Act 2003 places a duty on the chief finance officer (at this council the head of finance) to make a report to the council on the robustness of the estimates and the adequacy of the reserves. This report fulfils this requirement and provides councillors with assurance that the budgets have been compiled appropriately and that the level of reserves is adequate. It is a statutory requirement that councillors must consider this report when considering and approving a budget.

2. In presenting this report the head of finance is mindful of other associated statutory safeguards designed to prevent the authority from over-committing itself financially, namely:

    - Section 151 of the Local Government Act 1972 which requires the authority to make arrangements for the proper administration of its financial affairs and that the head of finance as chief finance officer has personal responsibility for such administration;

    - Section 32, 43 & 93 of the Local Government Finance Act 1992 which requires the authority to set a balanced budget;

    - The Prudential Code introduced as part of the Local Government Act 2003 sets out the framework within which the authority must manage its investments, including adequate planning and budget estimates;

    - The external auditor's duty to assess the adequacy of the authority's proper arrangements to secure economy, efficiency and effectiveness ('value for money').

3. To reinforce these obligations, section 114 of the Local Government Finance Act 1988 requires the head of finance as chief finance officer to report to all the authority's councillors, in consultation with the monitoring officer and chief executive, if there is or is likely to be unlawful expenditure or an unbalanced budget.

Robustness of the budget estimates

PREPARATION, REVIEW & SCRUTINY

4. In accordance with best practice and using accruals accounting, the council provides for realistic estimates of costs and known liabilities.

5. The detailed budget estimates have been prepared jointly by the heads of service and appropriately qualified from Capita's accountancy team. These have been reviewed and challenged by Capita's accountancy manager, the head of finance, the council's strategic management team (SMT) and members' budget working group.

6. The 2018/19 budget briefing session held with members on 6 February 2018 provided an explanation of the factors taken into account in determining the budget.

REVENUE BUDGET

7. The most significant costs within the revenue budget are:

    - staff salaries and related costs
    - payments under contracts for services
    - housing benefit and council tax support payments.

8. The estimates of staff costs are prepared by calculating the cost of employing each member of staff for the full year. The budget also includes the costs of recruiting to posts that are currently vacant, unless it has been decided that the post will not be filled. The costs include incremental progression and an allowance for the cost of any locally agreed pay award.

9. The risk of overspending on staff costs is therefore considered negligible. The risk of under-spending on staff costs is high and this year the council's policy has been to budget at 98 per cent of the expected salary level.

10. The costs of the most significant council contracts are linked to increases in the various price indices, usually the Retail Prices Index (RPI) or the Consumer Price Index (CPI). Allowance has also been made within the budget for additional costs arising from increased demand for services (e.g. additional properties leading to increased waste collection costs).

11. The risk of overspending on contract costs is therefore considered small. There remains a financial risk from a contractor failing to deliver services in accordance with the contract. Such risks are managed through the council's contract monitoring and risk management procedures, but cannot be eliminated.

12. The cost of housing benefit is largely met through government subsidy. The financial risk to the council should this cost increase significantly is small, because a very high percentage of the cost is met by the subsidy.

13. The level of local authority errors in the latest grant subsidy claim is safely below the government's threshold. The risk of any cost falling on the council is therefore low and continues to be mitigated by close contract management.

14. The government reformed council tax benefit from April 2013 when it became a local 'Council Tax Reduction Scheme' (CTRS). This change resulted in extra cost pressures for the council which have been factored into the proposed budget. The change also transfers the financial risk (and reward) from central government to the council for any significant changes in the numbers of residents claiming CTRS. We will closely monitor caseloads to assess any significant financial variation.

15. The areas of expenditure where there is a greater level of risk are within the demand led budgets such as the costs of homelessness (including temporary accommodation). Experience of demand in the current and recent years has been used to inform the 2018/19 budget.

16. As part of the budget setting process consideration has been given to income streams which could change as a result of recent and pending legislation. These include:

    - New Homes Bonus (NHB). Although the Ministry of Housing, Communities and Local Government did not make any changes to the NHB scheme for 2018/19 it has not ruled out a less generous scheme in future years. I have tried to be prudent in setting the NHB budget but future uncertainty cannot be avoided.

17. A number of revenue income streams are sensitive to changes in market conditions and therefore there will always be a risk that budget targets are not met. These include planning fees, building control fees, and land charges fees which all respond directly to the fluctuating characteristics of the housing market. Car parking income can also be volatile and responds to the general economy and retail market. Previous budget-setting exercises have made adjustments to reflect prevailing market conditions. Further adjustments have been made for 2018/19 refining budgets in light of actual patterns.

18. In order to minimise the risk of budgeted income not being achieved, the council takes a prudent approach when calculating the revenue income budgets and debts due and makes appropriate provisions for bad debts.

INVESTMENT INCOME

19. The returns on the council investment portfolio are relied upon to support the cost of services. The continuing impact of the low interest rates, and the predicted slow rise, have been factored in to the MTFP reported as part of the budget setting report.

20. Investments are diversified in accordance with the treasury management strategy, and the earnings assumptions in the budget are set prudently. Investment income is not committed until the year after it is earned. There is therefore certainty about the amount available when the budgets are set.

REVENUE CONTINGENCY SUM & OVERALL REVENUE BUDGET

21. Since 2014/15 I introduced a change to the way the council budgets for contingency. Previously underspends were in part caused by pessimistic budgeting that assumed and budgeted for worse case scenarios. A review of service budgets identified that, in addition to the central contingency budget, there were also budgets within services that could also be considered contingency budgets. These budgets have now been centralised.

22. There is now the potential for a greater call on the council's contingency budget and so the risk of overspending on this budget and the revenue budget has increased. Should this occur the council has adequate revenue reserves to cover such additional costs.

FUNDING FROM CENTRAL GOVERNMENT

23. On 19 December 2017 the government announced the provisional 2018/19 local government settlement. The final settlement was issued on 6 February 2018.

24. When calculating councils' spending power the Government assumes councils increase their council tax to the maximum level allowable before a referendum would need to take place.

25. The business rates retention scheme currently allows local government to keep fifty per cent of collectable income. From 2020 the government had proposed all business rates are retained by the sector. There is currently uncertainty over when the new scheme will start and whether it will be a one hundred per cent or a seventy-five per cent retention scheme. It is not possible to estimate the financial impact of any new scheme.

26. There is a risk that the assumptions about government grant reductions are proven to be under-estimated, in which case the council's revenue reserves are considered adequate to compensate until the MTFP can be reviewed.

CAPITAL PROGRAMME

27. The council has adopted a rigorous approach to the preparation of its capital programme. The split into an approved programme and a provisional programme is made to give greater certainty of costs and timescales before a final commitment is made. This requires a detailed appraisal to be agreed by the relevant cabinet member before expenditure is committed.

28. For major projects the council engages skilled advisors to assist it. Whilst these measures can manage and mitigate risks, by their nature some capital schemes will still contain significant financial risks. This is particularly the case with major redevelopments where the council may choose to be an active partner, sharing both risks and rewards.

29. In the capital programme recommended to the cabinet, allowance has been made for works considered necessary to the council's land and property assets.

30. In estimating additional capital receipts a view has been taken of the income to be obtained from future asset disposals.

31. The council has sufficient capital contingency and capital reserves to meet any potential capital overspends. While the use of these reserves would reduce the interest income earned, the impact would not be significant. The investment income is not committed until it has been earned.

MEDIUM TERM FINANCIAL PLAN

32. An updated version of the MTFP has been included in the budget report taking account of all budget changes since that date. The plan sets out provisional revenue spending plans and the estimated use of reserves through to 2022/23.

33. Over the past decade, the council has been at the forefront of new savings initiatives, for example joint working with the Vale of White Horse District Council to generate significant staffing savings. As a consequence, the council has been able to reduce its costs as government funding has reduced. In my report to council two years ago, I highlighted that the council's revenue expenditure would soon exceed its revenue income. This has happened and the council now has to draw on its balances in order to balance its budget.

34. In recent years, the government has encouraged councils to use their surplus balances before making cuts to budgets and has encouraged councils not to raise council tax through the awarding of council tax freeze grant.

35. The council has strong balances and so can support the revenue account across the entire five years of the MTFP. However, beyond that the council will need to eliminate this gap.

36. During 2018/19 the members' budget working group will review the medium term financial strategy to see how this funding shortfall can be addressed. The council is fortunate to have sufficient time in which to devise and implement a strategy to bring the revenue account back into balance.

PRUDENTIAL INDICATORS

37. The prudential code requires the calculation of a number of prudential indicators, which measure the sustainability of the council's MTFP, explicitly with regard to affordability, prudence, value for money, stewardship, service objectives and practicality. This is backed up by a specific requirement to monitor performance against forward-looking indicators and report and act on significant deviations.

BUDGET MONITORING

38. At the end of September and November heads of service complete budget monitoring returns forecasting their year-end positions. These are considered by SMT before being published in In-Focus.

RISK MANAGEMENT & INSURANCE

39. A risk and insurance officer is now in post, and the risk management arrangements are currently under review.

40. A new insurance framework is now in place, and the risk and insurance officer led a thorough review of the council's insurance arrangements. This fed into the annual insurance renewal process resulting in greater assurance that the council has comprehensive cover in place.

41. The main risks inherent in the council's MTFP are:

    - government grant funding being less than estimated
    - NHB income being less than that shown in the MTFP
    - substantial increases in council tax reduction scheme caseload and costs
    - macro-economic changes, such as slower interest rate rises, higher inflationary pressures and slower housing growth
    - Unforeseen growth in essential expenditure.

    There are sufficient usable revenue balances and New Homes Bonus income to allow time to manage the financial consequence of any of the above costs arising over the medium term should the risks materialise.

Adequacy of reserves

42. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued guidance on local authority reserves and balances in Local Authority Accounting Panel (LAAP) bulletin 55. It sets out the three main purposes for which reserves can be held:

    - A working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – which forms part of general reserves;
    - A contingency to cushion the impact of unexpected events or emergencies – also part of general reserves;
    - A means of building up funds often referred to as earmarked reserves, to meet known or predicted liabilities.

43. The council's Medium Term Financial Strategy (MTFS) states that the council will hold £50 million of investments of which £35 million can be invested in capital schemes that will produce a return of certainty. The remaining £15 million can be invested in treasury investments. Whilst the treasury investments are capable of being realised, investment in capital schemes is not capable of being realised.

44. Excluding the £50 million investment, the council is projected to hold £5.2 million of general revenue balances and £7.7 million earmarked revenue reserves as at 31 March 2023. Of the earmarked reserves £2.1 million represents NHB ring-fenced for affordable homes.

Conclusion

45. The budget estimates have been prepared following a properly controlled and professionally supported process. They have been subject to due consideration and the identifiable risks should be capable of management.

46. Overall, the level of reserves is adequate in relation to the proposed revenue budget and capital programme and the budgets are sustainable although the council now needs to review its medium term financial strategy as government funding continues to remain tight.

William Jacobs (Head of finance and chief finance officer) 13 February 2018