

**STATEMENT OF THE SECTION 151 OFFICER UNDER THE REQUIREMENTS OF SECTION 25 OF THE LOCAL GOVERNMENT ACT 2003**

**ROBUSTNESS OF BUDGET ESTIMATES AND ADEQUACY OF THE RESERVES - at September 20, 2007,**

**1 Introduction**

This Annex focuses on the two responsibilities under the Local Government Act 2003 for the Council's S151 Officer to report to Members on:

- the robustness of estimates, sections 4-6; and
- the adequacy of reserves, section 7.

This Annex builds on the statements made in setting the 2008-09 budgets. It will be further updated, for the full Council at its budget setting meeting in February 2008.

**2 Processes**

Budget estimates are exactly that, estimates of spending and income made at a point in time. This statement about the robustness of estimates cannot give a guaranteed assurance about the budget, but gives members reasonable assurances that the budget has been based on the best available information and assumptions.

In order to meet the requirement on the robustness of estimates a number of key processes have, or will be, put into place, including:

- the issuing of clear guidance to Service Areas on preparing budgets;
- Work is currently underway with Service Areas to pilot the budget and Risk Registers with Service Areas and to refine the approach;
- peer review by finance staff involved in preparing the standstill [base] budget i.e. the existing budget plus inflation;
- the use of budget monitoring in 2007-08 in order to re-align budgets with current demand, for 2008-09;
- a new medium term planning process that highlights priority services;
- a review via Corporate Management Board of proposed savings and their achievability;
- a member review and challenge of each Service Areas proposals for the budget
- review of the budget by the Leader, who is the responsible Executive Member for the budget;
- the Chief Financial Officer providing advice throughout the process on robustness, including vacancy factors, increments, avoiding unallocated savings and reflecting current demand and service standards (unless

standards and eligibility are to be changed through a change in policy);  
and

- Senior Managers reporting on the robustness of estimates to the Overview & Scrutiny Committee and subsequent scrutiny by that Committee.

Notwithstanding these arrangements which are designed to test the budget throughout its various stage of development, considerable reliance is placed on the Senior Managers having proper arrangements in place to identify issues, project demand data, and consider value for money and efficiency.

A key part of improving these processes is to develop data and information to monitoring service volume and unit costs and tracking changes in both. This will also assist in the Council's Medium Term Planning.

### **3 Risk Registers**

Finance are to undertake and provide a formal Risk Register of the Revenue, and Capital budgets at an appropriate level compared to the risks.

The development and introduction of these Risk Registers is not intended to replace the Council's existing Risk Register, rather that they should inform any revision of the Council Risk Register.

Capital Programme and Revenue Budget Risk Registers – by Service Areas, will be completed and approved by Service Area Management Teams by March 2008 following the final determination of both the Capital Programme and the Revenue Budgets for 2008-09.

The Risk Registers are intended to form part of the 2008-09 and onward Budgetary Control framework and used at Budgetary Control meetings with Service Area personnel and reviewed at least quarterly by Service Area Management Teams.

### **4 Robustness of Revenue Estimates**

The 2008-09 budget process will continue the trend of improving the Council's budget preparation, there will be choices for the Council in this respect:

- to increase financial resources to meet the increased demand and reduce the risk of overspending in 2008-09; or
- to reduce (where possible) service levels and standards, frequency of service delivery, eligibility for services and reduce the risk of overspending in 2008-09.
- To review the level of reserves against known and unknown risks

As part of developing the budget, members of the administration will have considered these options and they will be reflected in the proposed budget.

A small number of budgets will be re-based to ensure they reflect the withdrawal of grant income or income withdrawn from the Formula Spending Share, in addition to the management structure re-alignment..

The table below shows the factors to be taken into account in developing the draft budget.

Budget Assumption	Financial Standing and Management
<p>1. The treatment of demand led pressures</p>	<p>Four major demand factors affected the 2007-08 and later years budgets. They are:</p> <ul style="list-style-type: none"> <li>• Pay and Rewards – a recasting of the basis of pay is in negotiation. The modelling will and settlement is not yet finalised. The first payment will include a backdated payment to April 2007. The advice is that such exercises add 3-5% to the paybill. Therefore an estimate has to be included. For planning purposes, the mid-range 4% has been used.</li> <li>• NWLL – the arms length leisure trust ceased trading. The current prognosis is that further support will be required in 2007-08 and 2008-09. For planning purposes additional budget, to the base subsidy, has been included in those years. However this may not be sufficient to cover the new 'interim' arrangements as NWDC will continue to be liable for more risk during 2007/08 and 2008/09 than originally planned.</li> <li>• Management re-structure. This exercise commenced but did not complete due to the announcement of Unitary status, early indications are the savings assumed for 2007/08 and future years should still be achieved.</li> <li>• Other pressures – as yet not determined from the current year which will impact on the next year.</li> </ul> <p>All Senior Managers will have reviewed their base budgets including demand led pressures. Service Areas are expected to put forward management and policy actions to manage the additional demand within the relevant legislation either within the relevant budget or reprioritising within their Service Areas budgets. If this is not possible, and under-spending management action or policy actions in other Service Areas are not sufficient to cover the additional demand, then the minimum level of reserves may have to be used to address the additional expenditure temporarily.</p> <p>The 2008-09 budget will be based upon budget monitoring from 2007-08 and projections made by Senior Managers of demand in future years.</p>
<p>2. The treatment of inflation and interest rates.</p>	<p>Pay - 4.00% was provided in the 2007-08 budget for the pay award for staff, with 2.75% for 2008-09 . The current assumption is that there is no net increase in the paybill due to increments – this is to be tested.</p> <p>The employers pension contributions is at 26.1%. No increase was required for 2007-08. A revaluation will be undertaken in 2007-08, to take effect from April 2008. For planning purposes an increase of 1.0% per annum has been assumed for 2008-09 and 2009-10.</p> <p>The current vacancy factor [VF] built into the 2007-08 budget is 3%, which is broadly in line with that 'naturally' achieved. This excludes any areas where teams are so small as to make a vacancy factor impractical.</p> <p>Price inflation has been provided as follows:</p>

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Budget Assumption	Financial Standing and Management			
		2007-08	<b>2008-09</b>	<b>2009-10</b>
	Transport	3%	<b>3%</b>	3%
	Supplies & Services	2%	<b>2%</b>	2%
	Premises	3%	<b>3%</b>	3%
	Other Income	3%	<b>3%</b>	3%
	Government funding	actual	<b>2.5%</b>	2.5%
	Council Tax	3%	<b>3%</b>	3%
	Council Tax base	actual	<b>220 Band D's?</b>	220 Band D's?
	OR			
	Price inflation has only been provided on contractually or quasi-contractually committed budgets either at 2% or the rate stated in the relevant agreement.			
	Interest rates for 2007-08 are higher than anticipated, therefore investment income should exceed budget. It is therefore expected that the targets set for 2008-09 during the MTFP will be met			
3. Estimates of the level and timing of capital receipts.	This area is being reviewed and will be updated during the Budget Process with the Budget and Strategic Planning Working Group and Executive.			
4 The treatment of income	<p>LABGI – this Government reward, for increasing the Business base at a quicker rate than predicted, Further information is required to update the actuals for 2007-08 and so inform the expectation for 2008-09, which was nothing in the MTFP.</p> <p>Parking – financial impact of the restructure of car parking charges from 2007-08 will be reviewed and the budget assumption for 2008-09 updated.</p> <p>Toilets – whilst this was enacted in 2007-08 the full year effect is not yet known, and will influence the budget for 2008-09</p> <p>Other income – an annual uprating, to take account of inflation, is expected to increase other income by 3% overall.</p>			
5. The treatment of efficiency savings/ productivity gains.	All Senior Managers have a responsibility to ensure the efficient delivery of services and when efficiency savings are proposed that those savings are both realistic in terms of the level of savings and timing. Should the level and timing of such savings vary due to unforeseen events and under-spending, management action or policy actions within the relevant Service Area and corporately, are not sufficient to cover the variation, then the minimum level of reserves may have to be used to address the additional expenditure temporarily.			
6. The financial risks inherent in any significant new funding partnerships, major outsourcing deals or major capital developments	<p>The sharing of risk is in accordance with the principle of the risks being borne by the party best placed to manage that risk. Inherent risks include any guarantee or variation of service throughput (service volumes). If risks materialise the expectation is that such an eventuality will be considered in future years' budgets and general fund reserves restored to at least the minimum prudent level.</p> <p>Grants – the level of Grants and the contractual arrangements that underlie the partnerships, will be reviewed as part of the detail budget process</p>			

Budget Assumption	Financial Standing and Management												
7. The availability of other funds to deal with major contingencies	<p>The minimum level of reserves assumes that management and policy actions will be taken to address major contingencies. Should these be insufficient, the minimum level of reserves may have to be used temporarily and restored to at least their minimum prudent level or the optimal level through future budgets.</p> <p>The major risks facing the Council will be highlighted during the detail process and included in the final reports.</p>												
8. The overall financial standing of the authority (level of borrowing, debt outstanding, council tax collection rates etc)	<p>The Council has manageable debts, with just one loan for £4.000M..</p> <p>The assumed (ultimate) Council Tax collection rate for 2007-08 onwards is 98.2%, judged to be achievable, with further improvements anticipated in 2008-09 to achieve 98.5% or greater. For each 1% not collected, the cost is approximately £0.060m in lost income to the Council in 2007-08. Legislation requires that any collection fund deficit be corrected through the Council Tax in the next year.</p>												
9. The authority's track record in budget and financial management.	<p>The Council's recent track record in budget and financial management shows potential variations of +/- 1% of the net budget (equivalent to £186k on the Adjusted 2006-07 net budget):</p> <table data-bbox="531 907 1383 1041"> <thead> <tr> <th></th> <th></th> <th>Amount</th> <th>% of budget</th> </tr> </thead> <tbody> <tr> <td>▪ 2006-07 – Actual</td> <td>Adverse</td> <td>(£619k)</td> <td>(3.27)</td> </tr> <tr> <td>▪ 2007-08* – Forecast</td> <td>Positive</td> <td></td> <td></td> </tr> </tbody> </table> <p>* As projected at P4 monitoring</p> <p>Ultimately, financial performance relies on all budget managers and Senior Managers actively managing their budgets and complying with financial regulations, including not committing expenditure if there is no budget provision available.</p>			Amount	% of budget	▪ 2006-07 – Actual	Adverse	(£619k)	(3.27)	▪ 2007-08* – Forecast	Positive		
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▪ 2007-08* – Forecast	Positive												
10. The authority's capacity to manage in-year budget pressures	<p>The authority has improved its ability to manage in-year budget pressures. The following steps assisted; Re-set the rules for dealing with overspends, improved accuracy of estimates, deliver what was planned.</p> <p>However the lack of Improvement in the financial system itself remains a material weakness, this was due to be replaced in 2007-08, but due to the advent of Unitary will not be progressed.</p>												
11. The strength of the financial information and reporting arrangements.	<p>It has been recognised that the financial information and reporting arrangements needs to be strengthened. The Council needs to introduce commitment accounting, improve the usability of the system for non-financial users, and implement a single debtors system.</p> <p>Equally the turnover of senior finance staff has reduced the level of continuity and continues to affect capacity. The remaining team is seeking to restore this and improve the standards in all areas.</p>												

Budget Assumption	Financial Standing and Management
12. The authority's virement and end of year procedures in relation to budget under/overspends at authority and departmental level.	<p><i>To be reviewed</i></p> <p>The Council's virement and carry forward rules are clear. The Council is operating management disciplines to ensure management and policy actions are considered in relation to overspending budgets. Generally virement is considered at a corporate level against corporate priorities, including the contribution towards the optimal level of general fund reserves. The Council operates a policy of clawing back overspends from the relevant Service Areas in the following year – a discipline which needs to be maintained.</p>
13. The adequacy of the authority's insurance arrangements to cover major unforeseen risks.	<p>The Council's insurance arrangements are a balance between external insurance premiums and internal funds to "self-insure" some areas. External premiums are also managed by an excess payable by NWDC for claims received. Premiums and self-funds are reactive to external perceptions of the risks faced by the Council which includes both risks that are generic to all organisations and those specific to the authority.</p> <p>Both those issues produced large increases in risk and thus premiums/costs in recent years that required increases to reserves. Trend analysis indicates that these have now settled and provide confidence that no substantial increases in risks and costs should be seen in near future. But of course, by its very nature, insurance is a service that manages unforeseen risks, and reserve levels must be kept under constant review in this area. The recommended reserves strategy takes this uncertainty into account.</p> <p>The level of the Insurance Reserve has been reviewed for 2007-08 and 2008-09 will be reviewed to assess whether it can be judged to be adequate, the position being that estimated outstanding liabilities are covered by the balance on the Reserve.</p>

Taking into account the above and building on the work over the past 2 years, the proposed budget is expected to be more robust than in previous years.

## 5 Risk

In reports to the Overview & Scrutiny Committee during January 2008, all Senior Managers, with the support of their financial consultants, will assess the robustness of their budgets, the achievability of savings, income and reductions. It is expected that the key risks will be:

- Leisure and the level of support;
- Pay and rewards, the outcome of which is estimated;
- The management restructure;
- The Capital Programme, given any slippage in 2007-08;
- The Pension Fund revaluation, affecting 2008-09 onwards;
- Volatility of income in the Service Areas, especially the Planning Delivery Grant;
- Demographic trends being even slightly higher than projected or estimated;
- Changes in Housing Benefit funding and structure;

- Changes in policy or non-implementation of policy changes built into the budget.

These assumptions and potential changing circumstances will require the budget and forecasts for 2008-09 to be reviewed early in the financial year leading to more detailed budgets being prepared for the next financial year and the medium term during the autumn of each financial year.

## **6 Capital Budget**

Projects included in the capital programme, will be prepared by the Service Area project managers, with full adherence to the corporate project appraisal procedures and in line with financial regulations. All projects will be signed off by the relevant Senior Manager and Executive member with portfolio. The agreed programme is expected to be fully funded.

Projects will be costed at current year prices with many subject to tender process after inclusion in the programme. This may lead to variance in the final cost. In some areas, the design brief may not be finalised, again giving rise to potential price variance.

Service Area's are required to work within the given cash envelope so any under or over provision must be found within these limits.

The risk of the Council being unable to fund variations outside of the programme is minimal mainly due to phasing of projects. If necessary the Council can choose to freeze parts of the programme throughout the year to ensure spend is kept within the agreed budget.

The main risk to the capital programme is the ability of the Council to fully deliver it within the agreed timescales. Slippage relating to 2007-08 will be fully funded but this in itself will increase pressure on the Council to deliver the anticipated 2008-09 programme.

<b>Budget Assumption</b>	<b>Financial Standing and Management</b>
1. Estimates of the level and timing of capital receipts.	<i>[To be updated]</i>

## **7 Adequacy of the Reserves**

### *General*

Under the 2003 Act the Secretary of State has reserve powers to set a minimum level of reserves. The most likely use of this power is where an authority is running down its reserves against the advice of their Chief Financial Officer.

Determining the appropriate levels of reserves is not a precise science or a formula e.g. a percentage of the Council's budget. It is the Council's safety net for unforeseen or other circumstances and must last the lifetime of the Council unless contributions are made from future years revenue budgets. The minimum level of balances cannot be judged merely against the current risks facing the Council as these can and will change over time.

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Determining the appropriate levels of reserves is a professional judgement based on local circumstances including the overall budget size, risks, robustness of budgets, major initiatives being undertaken, budget assumptions, other earmarked reserves and provisions, and the Council's track record in budget management.

A budget strategy should also include a reserves strategy.

The consequences of not keeping a minimum prudent level of reserves can be serious. In the event of a major problem or a series of events, the Council would run a serious risk of a deficit or of being forced to cut spending during the year in a damaging and arbitrary way.

### *Unallocated General Fund Reserves*

During the CPA process, the following definition of adequacy was advanced:



### Audit Commission's measure of reserves

Either, the aggregate of the following items is expected to be in surplus at 31 March,

- General Fund balance;
- Other earmarked GF revenue reserves; and
- Liabilities not recognised in financial statements [excluding FRS17 unfunded pension liabilities]

and the GF balance is expected to be at least equal to 5%\*, [but not exceeding 100%] of forecast net operating expenditure. There are plans agreed by members on how to use these reserves, which link to the Council's strategic aims.

OR

There is a formal financial risk management process operating which the authority uses to:

- Justify a lower level of reserves;
- Determine its minimum level of reserves; and
- To adhere to this level.

\* Equivalent to £m for 2008-09.

The recommendation on the minimum prudent level and optimal level of reserves has been based on the robustness of estimate information (above). In addition, the other strategic, operational and financial risks taken into account when recommending the minimum level of unallocated General Fund reserves include:

- The Council will need to budget for provision for the cost of any redundancies necessary to achieve any budget savings and restructuring to the extent they are not continued in budget proposals. The Council's policy is that redundancy costs are 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. Senior Managers have been requested to be prudent in their assumptions and that those assumptions, particularly about demand led budgets, will hold true in changing circumstances.
- 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 (NWDC's threshold for 2008-09 has been set at £Y, 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.

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- Risk of changes from hypothecated grant to unhypothecated FSS.
- The unpredictability of the Formula Grant in the latter two years, which await the Spending Review 2007 announcements.
- 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.
- Potential short term differences between the Council's Insurance Reserve and outstanding liabilities, although these should be remedied in the following fiscal year.
- 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.

As a consequence, it is recommended that the minimum prudent level of general fund reserves is £Xm for 2008-09 and, an optimal level is £Ym to be achieved over the medium term.

The 3-year forecast and continuation budget include a contribution/use of Zm.

The recommendations of the Chief Financial Officer are: *[To be updated]*

- a) The Council maintains a minimum prudent level of general fund reserves of £Y.0m at the end of any financial year from 2007-08. The minimum level is designed to cope with unforeseen circumstances, which cannot be addressed by management or policy action within the year.
- b) That an optimal level of general fund reserves is £Zm. The optimal level of reserves is designed to allow the Council to withstand a measure of changes in circumstances during the year or minor variations in projected resources or spending over the period of a Medium Term Strategy;
- c) However the £Ym target does not represent a medium / long term safe level of reserves reliant as it is upon being able to accommodate just a single significant event. As this year has shown, putting budgets right, demands reducing services to achieve the approved budget, and is critical to the level of reserves and setting a realistic budget.
- d) A prudent approach would accommodate an ability to correct any single significant event over multiple years by creating a longer-term resilience. It also emphasises the need to ensure discipline over the clawback of overspends in future years.
- e) The reserves are currently £k above the General Fund unallocated reserves target.
- f) Based on that approach, a reserves figure of £Zm0 is recommended.