

### Section 25 report, Local Government Act 2003

- 1 Section 25 of the Act requires the Chief Financial Officer (the County Treasurer) to report to the County Council when setting its council tax on:
  - the robustness of the estimates included in the budget
  - the adequacy of the financial reserves in the budget.
- 2 The County Council is required to have regard to this report in approving the budget and council tax. It is appropriate for this report to go first to Cabinet and then made available to the County Council in making its final decision.
- 3 The CIPFA guidance on reserves and balances provides the general framework for considering the adequacy of reserves. Paragraph 15 of the report to the Cabinet outlined the provisional budgets for 2011/12 and 2012/13, set in the context of the County Council's medium term financial management policies. The 2010/11 budget is based on firm Government grant allocations, but these do not extend to 2011/12 and 2012/13 and therefore assumptions have had to be made on the implications for grant levels.
- 4 A risk assessment has been made of the cost and demand pressures on budgets, insurance liabilities, achievement of budget savings, adverse winter conditions and achievement of capital receipts which supports the proposed level of balances of approximately £17m. This assessment is set out as an Annex to the Appendix.
- 5 Similarly the level of reserves is scrutinised each year and the protocol on the purpose, use, control and review of each reserve has been agreed. Details of the protocol and the expected movements in each reserve were set out in Appendix 6 of the report to the Cabinet. Schools have one of the largest reserves at a projected £40.3m within their delegated budget and ring-fenced specific grant. The most important reserves for other services in terms of the three year view are the grant equalisation reserve (used to help match grant loss), the equal pay reserve and corporate efficiency reserve.
- 6 Section 25 concentrates on the uncertainty within the budget year rather than the greater uncertainties in future years. However the greater uncertainties extending beyond 2010/11, particularly for the County Council as a 'floor' authority also informs the need for reserves and balances beyond the period of the current three year grant settlement, together with the impact of equal pay claims, greater risks of overspend from tight savings targets and demand led spending pressures during a recession, potential higher inflation and slippage in the achievement of capital receipts.

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- 7 The budget report is the conclusion of a detailed process of prior consultation and consideration through out the current year by Cabinet.
- 8 The County Council's policy on balances is to hold a minimum prudent level which on the basis of 2010/11's risk assessment is 2.3% of net expenditure. This is a higher level than has been necessary historically but comparable with 2008/09 and 2009/10, when balances were budgeted at similar levels, and remains relatively low compared with other equivalent local authorities. The risks associated with being a floor authority and thus receiving the minimum increase in government grant and of needing to achieve significant savings in service expenditure to balance the budget continue to justify a higher level of balances than historically. In other respects the risks have changed over the last twelve months, as the rate of economic decline has slowed, and the banking system has been stabilised. Of greater concern in 2010/11 is the prospect of much lower public spending provision from 2011/12.
- 9 The level of uncertainty for the budget year is narrowed down as the budget strategy is developed during the year and defined in the performance and risk management and earmarked reserves paragraphs in the budget report.
- 10 In setting the budget the County Council should have regard to the strategic, operational and financial risks facing the County Council. The County Council has an overall risk management framework which covers these issues. The forward budget plan and reserves take into account the main risks and uncertainties, including:
  - Inflation
    - the 2009 Local Government pay award was settled at 1% and the local authority employers have proposed a pay freeze in 2010/11.
    - price inflation has been set at 2.25%. This is likely to be broadly sufficient in 2010/11 with a number of longer term contracts indexed to the RPI/CPI having low increases or reductions this year.
    - short-term interest rates have been budgeted to average 1% in 2010/11, 0.5% above the current base rate, as an upward movement in base rate is expected to begin during 2010/11.
  - Pay drift
    - increments are not budgeted for and services will need to secure efficiency savings to offset these. Past trends suggest that this can be managed, and service budgets have been adjusted for the impact of the new pay structure.
    - there is a substantial potential liability from equal pay claims arising from the pay and benefits review. None of the claims has yet been considered by the employment tribunal and an

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equal pay reserve estimated at £41.6m at 31 March 2010 has been built up for non-school claims. School balances will assist in meeting claims in respect of school-based staff. An application for a capitalisation direction will be made in 2010/11 to protect against the risk of successful claims exceeding the capacity to fund them from the relevant reserves. A settlement in excess of this figure will require a capitalisation direction to enable the revenue impact to be phased over more than one financial year in order to avoid compensating job or service cuts, though there is no guarantee that the Government will provide an adequate capitalisation direction. The Government has also taken steps to assist local authorities to spread these costs by introducing regulations which allow the effect of accruals for equal pay liabilities to be disregarded for council tax setting purposes.

- The budget for 2010/11 takes account of an increase of 0.5% in the employers' pension contribution to the Local Government Pension scheme, expressed as a percentage of pay. This is based on the outcome of the actuarial valuation at 31 March 2007 and the position for 2011/12 will not be known until after the next actuarial review as at 31 March 2010. Taking into account new consultation proposals from Communities and Local Government and the constitutional permanence of local government, it is anticipated that employer rates will be contained at the current level from 1 April 2011.
- Additional spending, savings and redeployments built in to the budget
  - these are subject to planned review by Executive Members, and savings plans will need to be approved and monitored during the course of the year.
- Efficiency savings and other savings
  - there is a good track record covering the process of setting and achieving savings, but the national target for local authorities has increased in 2010/11 to 4% and it may become more difficult to continue to achieve year on year improvements on the scale required to meet the target.
  - previously most efficiency savings have been redeployable within service budgets, but from 2011/12 a corporate target of £15m per annum has been set in response to forecast reductions in Government grant. Advance savings of £8.6m are budgeted in 2010/11 to be transferred to an earmarked reserve.
- Income

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- there is an annual review to maximise income and increase income at least in line with costs which is referred to in paragraph 6 of the report to the Cabinet and reported in greater detail to executive members
- Achievement of budget plan
  - There is a well established and sound history of very close achievement of outturn to budgets, and though Children's Services are predicting an overspending in 2010/11, action is being taken to limit the scale of the potential overspending.
- \* Strength of financial information and reporting arrangements
  - budget monitoring and control is well established, particularly in reporting and taking action over the second half of the financial year. Corporate co-ordination of budget monitoring focuses on demand led budgets, overall employee budgets and the achievement of planned savings.
  - other action plans have been put in place to consolidate and improve financial controls, including the monitoring of financial health indicators.
- Capital programme
  - capital strategy, asset management plans and the local transport plan have all previously been accredited with the highest scores in the former comprehensive performance assessment.
  - the slow down of the property market has produced a temporary shortfall of capital financing resources in 2008/09 and 2009/10. Additional revenue contributions to capital were made in both in 2008/09 and 2009/10 and allowance has been made in the budget for additional temporary unsupported borrowing to cover the immediate shortfall.
  - the policy on Government borrowing approvals was reviewed in 2007/08, because as a council at the grant floor, additional 'supported borrowing' is not being matched by increased revenue support grant. Restricting the automatic take-up of supported borrowing to a level which will limit the increase in the capital financing requirement relating to supported borrowing to 2.5% per annum will have a continuing impact in containing increased capital financing costs.
- Level of borrowing and outstanding debt
  - the issues are fully covered in the treasury management strategy and prudential indicators ( Appendix 1 of this report).
  - the current policy on temporary unsupported borrowing for specific projects results in the financing costs being

contained within the forward budget plan cash limits without an additional impact on the council tax payer.

- however despite much lower capital receipts in 2008/09 and 2009/10 than originally planned, it has been possible to avoid the need for temporary unsupported borrowing to cover a general shortfall in capital financing resources.

\* Contingent Liabilities

- the County Council self-insures, so it finances all its own liability claims. The liabilities are uncertain but to cover these a provision is maintained for known liability claims and a reserve is maintained to deal with fluctuations in liabilities and in the level of fire damage reinstatement, which now stands at £9.3m.

• Annual Governance Statement

- the Treasurer has the responsibility for ensuring that an effective system of internal financial control is maintained and operated in connection with the resources concerned.
- the review of the effectiveness of the system of internal financial control is informed by the work of the managers within the County Council, by internal audit and the Audit Commission in its annual governance report and other reports.
- the Audit Committee receives and reviews the annual governance statement and the external audit governance report.

• Audit Commission

- gave an unqualified opinion on the 2008/09 accounts, and assessed the County Council's financial planning at Level 4 in the 2009 Use of Resources assessment.

• Other risks

- there are potential legal claims outstanding and other possible risks which past trends suggest can be met from balances if required. There is no known significant risk or liability which requires a provision, contingency or reserve not already allowed for in the budget report. The main new risk for which contingency provision has been made arises from the possible introduction of a duty to provide free personal home care, irrespective of means, to people meeting the care assessment criteria from 1 October 2010.
- changes in function and funding arrangements. There are no significant externally imposed changes in 2010/11, with the

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exception of the third phase of the transfer of the student support service to the Student Loan Company.

- though government grants have been confirmed for the next year, the County Council's formula grant calculated from the formula is still £20.7m below the grant floor in 2010/11. The proposed policy on the use of the grant equalisation reserve will provide some scope to mitigate the immediate impact of further grant loss beyond 2010/11.

- 11 Provided that the County Council considers the above factors and accepts the budget recommendations, including the level of earmarked reserves and balances, a positive opinion can be given under Section 25 on the robustness of the estimates and level of reserves.

Jon Pittam

County Treasurer

27 January 2009

**2010/11 – RISK ASSESSMENT OF GENERAL BALANCES**

Cash- limited expenditure (exc. schools)		Inflation					
		Inflation	Pay	331,396	0.25	828	Possible risk of national pay awards exceeding lower pay award assumption.
Pay	325,473	5,923	Non pay	566,443	1	5664	Allowing for potential for absorption within cash limit.
Non pay expenditure	555,769	10,674	Income	-197,799	-1.25	2472	Risk of resistance to income generation assumption.
Income (includes inf on specific grants)	191,803	-5,996					
			Interest rates	18,625	5	931	Short term interest rates may increase in 2010/11 above current level but majority of interest costs on long term fixed rate borrowing.
Base budget	689,439	10,601					
Growth in budget strategy	8,260		Demand led	266,921	6	16,015	Allowing for potential for absorption within cash limit.
Growth funded from redeployment	1,967		budgets				
Further growth proposed	0		Insurance	4,925	25	1,231	
Balance of contingency allocation	13,474		liabilities				

Capital financing - principal	23,876	Achievement					
- interest	18,625	of cashable	21,819	20	4,364	Risk affected by scale of savings targeted.	
Flood Protection/Coroners	1,530	savings					
RCCO	16,799	Capital	12,951	10	1,295	To reflect possible reduction in values rather than delay.	
Specific grants (exc. schools)	-98,946	receipts					
Reserve contributions	-9,196	Winter maint'e	3,342	25	836	Risk of adverse winter conditions borne from balances.	
LEA contribution to schools budget	128						
Revised pay assumptions	-4,428	VAT - partial					
		exemption	1,500	5	75	Low risk based on 2008/09 assessment.	
		(exc schools)					

**BUDGET REQUIREMENT 672,129**

Demand sensitive budgets

Older people placements	111,710		
Physical/ sensory	21,301		
Learning disabilities	71,246		33,713
Mental Health	7,038		
		Less likelihood of worst cases coinciding	50 16,856
Home to School transport	24,601		
Looked after children	21,349		
		<b>Proposed target balances</b>	
Bus subsidies	8,388		<b>16,856</b>
Abandoned vehicles	31		
Coroners	1,257		
	266,921		

Insurance liabilities	4,925
Winter maintenance	3,342
Business rates	4,053
Capital receipts	12,951