Cheltenham Borough Council
Cabinet – 8 February 2011
Council – 11 February 2011
Section 25 Report

Accountable member	**Cabinet Member for Community Development and Finance, John Webster**
Accountable officer	**Section 151 Officer, Mark Sheldon**
Accountable scrutiny committee	**all scrutiny committees**
Ward(s) affected	**All**
Key Decision	**Yes**
Executive summary	This report fulfils the requirement under Section 25 of the 2003 Local Government Act for the Section 151 Officer to make a report to the authority when it is considering its budget, council tax and housing rents covering the robustness of estimates and adequacy of reserves. The Act requires Councillors to have regard to the report in making decisions at the Council's budget and council tax setting meeting.
Recommendations	**1. That Cabinet / Council consider this report in agreeing the budget and level of council tax for 2011/12.**

Financial implications	As contained in the report and appendices. **Contact officer: Mark Sheldon.** **E-mail: *mark.sheldon@cheltenham.gov.uk*** **Tel no: 01242 264123**
Legal implications	There is a legal requirement under Section 25 of the 2003 Local Government Act for the Section 151 to prepare a report to council. **Contact officer: Peter Lewis** **E-mail: peter.lewis@tewkesbury.gov.uk** **Tel no: 01684 272012**
HR implications (including learning and organisational development)	HR implications are outlined in the main budget report. **Contact officer: Julie McCarthy** **E-mail: julie.mccarthy@cheltenham.gov.uk** **Tel no: 01242 264355**
Key risks	See risk register at Appendix 1 of the main budget report.

Corporate and community plan Implications	See main budget report.
Environmental and climate change implications	See main budget report.

1. Background

1.1 The purpose of this report is to fulfil the requirement under Section 25 of the 2003 Local Government Act for the Section 151 Officer to make a report to the authority when it is considering its budget, council tax and housing rents covering the robustness of estimates and adequacy of reserves. The Act requires Councillors to have regard to the report in making decisions at the Council's budget and council tax setting meeting.

2. Robustness of the estimates

2.1 In drawing together the detailed revenue budgets for each service a number of assumptions and principles have been applied. In reviewing the overall robustness of the estimates these should be assessed.

Inflation

2.2 At the time of preparing the budget the inflation allowances built into the base figures for 2011/12 were a reflection of the available indices with an allowance to reflect the expected trend into 2011. The September 2010 rates for the 'Consumer Prices Index' (CPI) was 3.1% and for the 'All Items excluding Mortgage Interest Payments' (RPIX) was 4.6%. The latest indices available for December 2010 are for CPI 3.7% and for RPIX 4.7%. Contract inflation has been allowed for at the appropriate contractual rate e.g. utilities budgets reflect negotiated rates.

2.3 In line with previous practice, general inflation has not been provided for unless the relevant professional officer has indicated that there are inflationary pressures. Whilst this creates natural efficiency saving across the Council, it will be important to continue to monitor this policy to ensure that budgets are sufficient to provide services.

2.4 **I am confident that service managers have sufficient budgets to fund supplies and services based upon prevailing pay and price levels in 2011/12.**

Employee costs – pay / turnover

2.5 In line with government policy, employee budgets for 2011/12 do not allow for a pay award but do allow for contractual incremental progression for some staff that are below the top of their grade. The net cost of service assumes an employee turnover saving of around 3% of gross pay budget which equates to an estimated annual saving of c£400,000. Based on previous year's experience this has been achieved but, given the current economic situation and the impact of the job market on turnover, this needs to be closely monitored.

2.6 Currently the unions are lobbying for a pay award for lower paid workers for a flat rate of £250 for those earning under £21k per annum. This would cost the authority around £88k. Given the financial settlement and the uncertainty over whether this will be supported, no budgetary provision has been made for this. Had this been built into the budget, additional savings with potential staffing implications would have had to be made. The decision to deal with any financial consequences of an agreement above a pay freeze within the revised budget for 2011/12 is prudent given the uncertainty and implications of allowing for it.

2.7 Given the government proposals that pay is actually frozen for the following 2 years, the MTFS projection does not include any provision for 2012/13 or 2013/14 but allows for pay awards for the remainder of the period of the MTFS at 2%. Given inflationary pressure and a prolonged period of pay freeze there is likely to be upward pressure on pay.

Employee costs – pensions

2.8 The budget addresses the result of the triennial revaluation of the pension fund in 2010. Having built in the provisional additional contribution level increase notified by the actuary in the interim budget proposals, the revised position of the actuary i.e. stepping up to the increase contribution, allowed the Cabinet to make changes to its proposals. The changes allow for the saving to be used for one-off purposes in 2011/12. The resulting changes made to final budget proposals for 2011/12 ensure that the budgetary provision for the increase in pension contribution in 2012/13 is embedded into the base budget without further adding to the funding gap. This is a prudent approach.

2.9 The MTFS allows for further increases in contribution rates for the new triennial revaluation. The Government's Hutton review of pensions may conclude that the current public sector pension scheme is unsustainable and changes to the scheme may be made making it less generous and less expensive but will require legislative changes. However, the MTFS currently allows for further increase in pension costs as a result of a revaluation in 2013 reflecting the uncertainty in the economy and fund performance which may be offset by pension changes. Given the uncertainty over the outcome and timing of any changes, the approach to the MTFS is not unreasonable.

2.10 **I am satisfied that the Council has sufficient budgetary provision for employee related costs in 2011/12 and is being prudent in planning for potential future increases in pay and pension fund costs in the MTFS.**

Treasury Management

2.11 The Council signed up to the CIPFA Code of Practice for Treasury Management in 2002 and updates annually its Policy and Strategy statements accordingly. Its decisions are supported by an external consultancy (ArlingClose) and considered by the Treasury Management Panel.

2.12 Despite treasury management activity generating significant returns for the Council in the past, the sustained low level of interest rates would suggest that previous levels of investment income will not return for some considerable time. The level of investment interest earned by the Council is now budgeted at c£170k (a reduction from c£1.5m per annum before the recession). The Council has reduced the reliance on investment interest to support the net budget and in turn reduced the risk and impact of the volatility of interest rates on the budget.

2.13 No assumptions are made in the MTFS in respect of higher investment returns resulting from a potential increase in interest rates. Once the longer term situation becomes clearer, a more optimistic view may be reflected in the MTFS. The financial implications included in the budget are based on the recommendations of the Treasury Management Panel supported by Arling Close.

2.14 The collapse of the Icelandic banks (in which the Council had deposits of £11m made in 2006 for fixed three-year periods) presented a significant challenge for the Council. At this stage £1.6m has been returned to the council leaving £9.4m still to be recovered.

2.15 Currently the Council is awaiting the outcome of court test cases in Iceland, challenging the Winding-Up Board (wWUB) of Glitnir bank's decision to treat local authority deposits the same as other depositor's rather than give them preferential depositor status as had been determined by the WUB of Llandsbanki bank. There is currently no evidence to suggest that the level of losses may increase. The third bank in which the council made investment, Kaupthing, Singer and Friedlander, is now predicted to pay out more than originally anticipated. Given the uncertainty over the final outcome, the decision to make no further provision for losses in the budget is not unreasonable.

2.16 Following the banking collapse, the Chartered Institute of Public Finance and Accountancy (CIPFA) reviewed the Code of Practice covering this area and the Council revised its Treasury Management Policy and Annual Investment Strategy to take on board the recommendations of the review which strengthen the security of public money. The Annual Investment Strategy determines the parameters within which Officers undertake daily treasury management decisions. Following the banking crisis, the Council's treasury advisors, ArlingClose, continue to work with the Council and the Treasury Management Panel and provide on-going advice on policy.

2.17 In February 2009, a number of recommendations were incorporated in the revised Treasury Management Policy and Annual Investment Strategy's lending criteria to a much smaller lending counterparty list which was approved by the Council. Following advice from ArlingClose there is a proposal to increase the lending period to 2 years for some banks. Given that the council is now lending to only a very limited number of banks approved by ArlingClose, I consider this to be a reasonable relaxation in the lending policy which will not open up further risk to the Council.

2.18 The prudential code requires that certain calculations be made (prudential indicators) which measure the impact of treasury and borrowing decisions and these are included in the Annual Investment Strategy. The indicators for 2011/12 include the implications of the borrowing for the Gloucestershire Airport to finance the runway safety project, borrowing to support the financing of the refurbishment of the Everyman Theatre, borrowing to support the redevelopment of St Pauls by CBH and the implications on financing resulting from moving to International Financial Reporting Standards (IFRS) which require all forms of borrowing, including leases, to be included in the prudential borrowing limits. I am comfortable that the treasury related decisions, as measured by these indicators, are in accordance with the prudential code. The Council's Minimum Revenue Position policy statement supports the borrowing decision in respect of the Airport and the Everyman.

2.19 **I am satisfied that, given the prevailing low interest rates, the assumptions for budgeting for investment interest and potential Icelandic bank losses are reasonable and follow Government advice. In addition, given endorsement of the lending list by ArlingClose, the slight relaxation in deposit terms in the Annual Investment Strategy are appropriate and represent a tolerable increase in risk.**

Income, Charging and Demand.

2.20 The Council continues to provide a number of demand led services e.g. car parking, land charges, leisure@cheltenham etc. The estimates for 2011/12 have been prepared on the advice of the professional Officers who have taken a realistic view about income levels, taking into account the continued impact of the economic downturn. Income from development control and land charges remains suppressed and income budgets for 2011/12 have been prepared on this basis. No assumptions have been made in the MTFS in respect of improving income levels. Given the uncertainty over how long the downturn will last this is a reasonable approach to take.

2.21 Car parking income remains one of the Council's largest demand led risks. Given the sustained shortfall in car parking income revenues over recent years, the budget estimates for 2011/12 allow for a reduction in target by £500k and reflect the freeze in car parking charges.

2.22 The Council operates in some highly competitive areas where fees are subject to commercial decisions which are supported by benchmarking against the competition. The Council needs to be able to respond to the market and be 'business like' and as such, although fees and charges are proposed in the final budget, changes to fees and charges are not restricted to the annual budget meeting. This is particularly relevant in light of the MTFS funding gap projections and the work of the 'Bridging the Gap' (BtG) Programme which includes work streams for closing the funding gap from increasing income by increasing prices above inflation or the identification of new income streams, taking into account comparable charges with neighbouring authorities. Given the lack of Government funding, whilst being mindful of the impact on customer in the current economic climate, it is more important to maximise income levels and, as such, service managers need the flexibility to vary charges to maintain demand for services.

2.23 Over a number of years, the Council has benefited from sizeable amounts of Housing and Planning Delivery Grant (HPDG). As a result of the funding squeeze, this will no longer be received by the council. As such, given the desire to retain the current level of planning service, the Cabinet have built £130k into the base budget to cover the recurring cost of funding the residual posts being historically funded from this source.

2.24 **Overall, I am satisfied that the estimates for income are based upon reasonable assumptions made by Officers and which take into account the sustained underperformance of car parking income targets recognising the difficulty in predicting income streams in the current economic climate. Monitoring of income levels will be undertaken during 2011/12 and reported in the quarterly budget monitoring reports.**

3. Housing related budgets

Housing Revenue Account

3.1 The Council's Housing Revenue Account (HRA) capital programme and revenue account have been prepared in consultation with Cheltenham Borough Homes (CBH). They are in line with housing rent limits, and take into account the full year financial impact for both the General Fund and the HRA of the additional borrowing consents received to support meeting the decent homes standard.

3.2 The estimates take into account a revised estimate of the charges to CBH for Council services which continue to be refined annually to take account of the management agreement. The estimates have been drawn up based on the latest information available concerning relevant subsidy levels, expected mid year Capital Financing Requirement, and borrowing capacity (item 8 debit and credit calculations).

Housing and Council Tax Benefit.

3.3 The housing benefit regulations are changing and given the potential for unemployment levels to rise as a result of the government approach to tacking the deficit, the budget for benefit activity may become a higher risk area. This is one of the few areas where external audit is required to undertake a separate annual audit of subsidy, payments and claims work. As Members will be aware, given the size of the financial amounts involved (c£40m), this is always an area of concern in preparing budget estimates. The Council continues to improve its standards and monitoring procedures in this area. Sound processes are in place to manage this complex area of activity which supports accurate budgeting and control. Based upon the year end position for 2009/10 and the monitoring of the current year's budget I believe the budgets (as far as can be predicted in this very volatile area), are sufficient to fund predicted activity levels.

3.4 **In summary, the estimates for the HRA and Housing General Fund related budgets, as far as can be reasonably determined, appear to be robust.**

4. Finance Settlement

4.1 The estimates for 2011/12 provide for the financial settlement notified to the Council by the Department for Communities and Local Government (DCLG) resulting from the Government's Comprehensive Spending Review (CSR10) providing estimates for the Government support for the 2 year period 2011/12 to 2012/13.

4.2 In the coalition Government's comprehensive spending review in October 2010, the Chancellor of the Exchequer announced that councils would receive a cut in government support of 7.1% in each of the next 4 years, a total of 28.4% (which was broadly in line with the assumptions for a reduction in government support modelled in the Council's MTFS). The actual settlement results in a cash reduction in government support (revenue support grant plus share of redistributed non domestic rates) of £1.09m, a cut of 15.16% in 2011/12 followed by a further cash cut of £579k (9.57%) in 2012/13. Cumulatively, this equates to a 23.86% cash cut over 2 years.

4.3 The Council accepts that, through the reduction in government funding, it will play its part in tackling the level of national debt. However, in order to be able to respond appropriately and plan effectively, the Council needs clarity over the actual scale of cuts and timescale. The delays and lack of clarity over the size of the cuts have created a great deal of uncertainty which has added further pressure to a very difficult budget setting process. The Council has made representation to that effect through the response to the provisional settlement in December 2010 and via Martin Horwood MP. In particular, the ministers new measure of government support, 'revenue spending power' (CBC's spending power is reduced by 6.03% in 2011/12), the Council had not been notified that is was basing its estimates on this new measure until the provisional settlement in December.

4.4 Some Members have raised concerns over the lack of published papers prior to the Cabinet and council tax setting meeting making it difficult for members to submit questions. The lateness of this year's settlement presented particular difficulties which will hopefully not be repeated. However, in agreeing the budget strategy for 2012/13 budget I will review the timetable and budget setting process with members to ensure that members concerns are addressed.

4.5 In addition, the Council anticipated that it would receive funding levels for the life of the Parliament. The lack of clarity over future years adds greater uncertainly to the MTFS forecasting and planning. The MTFS projections now assume a further 5% cut in cash grant for the following 2 years.

4.6 The transfer in responsibility for administration of concessionary fares from district councils to the higher tier from 1st April 2011 takes away the uncertainty of costs and funding pressures from the Council. Despite responding to the settlement consultation the final settlement removed the total costs of £2.2m for concessionary fares including the local discretions i.e. 9:00am to 9:30am and taxi vouchers. As Section 151 Officer I have met, along with the Cabinet Member for Finance, Martin Horwood MP to lobby for the retention of the estimated £171,000 cost of the local discretions funded by the Council. Whilst there may be a possibility that this may be rectified in the future no assumption has been made as such in the budget proposals.

4.7 **Based upon the CSR10 settlement, the projections in the MTFS allowing for further reductions beyond the next 2 years is a prudent approach. Based upon the uncertainty over the outcome of any lobbying over the discretionary element of concessionary fares, the budgeting approach is sensible.**

5. Medium Term Financial Strategy (MTFS) and strategy for 'Bridging the Gap (BtG)'

5.1 Sound financial management requires that the Section 151 Officer and Councillors have full regard to affordability when making recommendations about the local authority's future revenue and capital programme. The Council produces a Medium Term Financial Strategy (MTFS) which assists in its planning and preparing for future potential liabilities. The budget proposals include an updated MTFS which is based on known or expected expenditure plans for 2012/13 onwards, together with a number of assumptions over the next 5 years. The MTFS predicts the funding gap for the next 5 years modelled using various funding scenarios.

'Bridging the Gap' (BtG)

5.2 The Council's 'Bridging the Gap (BtG)' programme outlines the Council's strategy for closing the funding gap which has undoubtedly helped to strengthen the Council's approach to longer term financial management. The BtG programme board meets monthly with the Cabinet Member for Finance which ensures that tackling the budget problem remains high on the Council's agenda. This approach has meant that in approaching the 2011/12 budget, the Cabinet have avoided salami slicing to close the funding gap. The BtG programme has delivered savings and additional income to meet the funding gap of £2.8m for 2011/12 and £3.8m over the period of the MTFS. My assessment of the progress and robustness of the BtG work streams is as follows:

Procurement savings

5.3 The budget proposals for 2011/12 and the MTFS do not now include a target from procurement savings. Whilst a programme of procurement projects/savings has been identified, given the pressure on procurement resources and the difficulty in turning procurement savings into recurring cashable savings, it was agreed that the target should be removed from the 2011/12 budget and MTFS. However, SLT have agreed that a procurement target should still be in place outside the MTFS and that SLT will work with the Procurement Officer to translate procurement activity into cashable savings, to be monitored by the BtG programme. This is a completely reasonable position to take given that the Council may have exhausted its own individual purchasing power in driving out procurement savings and the impact of rising prices. However, looking ahead, the GO shared Enterprise Resource Planning (ERP) system should help to deliver future shared procurement savings.

Asset Management:

5.4 Significant progress has been made in the delivery of the Asset Management Plan. Some key successes include the sale of some buildings that were surplus to Council requirements generating £638k of capital receipts which were used to deliver a £75k annual saving to the revenue budget and support the financing of the capital programme. Work on reducing the cost of utilities in buildings through optimising fuel usage will also make a valuable contribution over the period of the MTFS. The recent commencement of the process of sale and redevelopment of North Place and Portland Street car park could help to pump prime investment into the public realm.

Shared services:

5.5 The Council has made significant steps forward in progressing the shared services agenda. The Council now successfully shares legal and building control services with Tewkesbury Borough Council and works collectively on joint core strategy work. The partnership with Cotswold and West Oxfordshire for audit is also, whilst still in its infancy, gaining momentum. The sharing of an ERP and the establishment of a shared services for Finance and Procurement, HR and payroll services will follow shortly. It is evident that the work to implement shared services successfully is significant and should not be underestimated. The GO project is clearly a critical project since it provides the technology platform for other shared services and the Council must ensure that resources are not diverted from its implementation. Similarly, the establishment of a shared waste service with Tewkesbury Borough Council and rolling out the new waste and recycling service will require significant organisational effort.

Systems thinking / Service Reviews:

5.6 Some progress has been made in a number of areas resulting in savings targets for ICT and revenues and benefits being built into the budget for 2011/12. Translating systems thinking interventions into savings often requires a service restructure and the work required to fully deliver saving should not be underestimated. The early conclusions from initial systems thinking work has been very encouraging with suggestions that significant improvement in services can be achieved at the same time as making savings. It is important for the Council to learn from these early systems thinking / service reviews and should roll out the systems thinking approach across the organisation so that all services benefit.

Commissioning:

5.7 Now that Members have approved the decision to establish the Council as a commissioning authority, it needs to ensure that the programming of activity dovetails in with other BtG work streams and the timing of the commissioning programme is logical e.g. drive out systems thinking savings before commissioning. In approaching commissioning, services need to understand more clearly how they compare with other councils and other providers. Looking ahead, I am committed to working with SLT to begin to undertake ‘value for money’ assessments for all services and to use the budget working group of members to facilitate the debate over what level of service the organisation wants and can afford in future.

'One off' staffing costs

5.8 Members need to be mindful that, in making decisions to reduce staffing numbers, savings may not be delivered immediately since one off redundancy / pension costs may offset savings initially. The level of the General Reserve is not sufficient to meet significant one off costs. In the final budget proposals, many of the savings have been delivered as a result of vacancies which have been actively managed across the organisation. Careful workforce planning and vacancy management has been key to ensuring minimal impact on the General Reserve in 2011/12. Looking ahead, SLT need to ensure that they work collectively to look for redeployment opportunities to avoid redundancy costs and opportunities to manage workforce levels down in line with assessment of future BtG and commissioning work plans.

Future approach /capacity

5.9 In developing the BtG programme, SLT have collectively supported both the Cabinet and I in developing options for consideration in meeting the funding gap for 2011/12. This approach has been successful but has been extremely time consuming and the options now being suggested are often politically very difficult since they inevitably result in a cut or loss in service and are quickly rejected. Given the significant level of cuts required and the difficulty in avoiding hard decisions Members are urged to develop cross party consensus on more significant issues, possibly through the cross party budget working group.

5.10 The BtG programme contains some 93 separate work streams. Some of these will be delivered as a result of setting the budget but some still require significant effort and energy to deliver in both 2011/12 and future years. As part of the monitoring of the programme, officers will be undertaking more effective risk assessments of individual work streams to highlight any delivery issues. In tackling future year's budget gaps, Members need to be mindful not to add significantly to the programme of activity and to focus attention on fewer big ticket items. Opportunities to maximise income should be considered.

5.11 In moving to a commissioning authority, the council set aside £80k to support the significant amount of business change that the council is undertaking. SLT have undertaken some work on resource planning which should inform the council on where to direct this valuable source of funding.

5.12 Overall, the BtG programme continues to be an effective, collective approach for the identification and delivery of the savings and additional income required to bridge the funding gap for 2011/12, without significant impact on service levels or reverting back to 'salami slicing'. However, Members need to be mindful of the capacity to deliver other significant projects / work streams without additional resource.

Level of council tax increase

5.13 The final budget proposals assume a council tax freeze for 2011/12 which is in line with the Government aspiration. This will cost the Council c£197k in lost income based on the originally planned council tax increase of 2.5%, but this will be offset by specific grant from the government, guaranteed for 4 years. The alternative approach would have been to increase council tax up to the government cap, for which a new regime is being developed based on a maximum revenue spend (for CBC this is estimated at £15.1m, some £0.9m more than the £14.25m proposed budget) At a council tax increase of 2.5%, the Council would have been no better off since it would have lost the £197k additional grant and would still have had to make £2.9m of savings. At a council tax increase of 5% (which is unlikely to have been unacceptable in the current climate), the council would have only been around £197k better off. Any increase above 5% up to the new expenditure cap would clearly not be acceptable or worth considering.

5.14 The MTFS models the 4 years of support for freezing the council tax and the impact of its withdrawal. Over this period, pay and price level will increase which could be offset by future potential tax increases. Members need to be mindful in considering future council tax increase of the impact on the MTFS and avoid opening up the funding gap further in future.

5.15 Given the support offered by the government in freezing council tax, the decision to freeze council tax is reasonable.

Asset Management Plan (AMP) and Capital Strategy (CS)

5.16 Sound asset management planning is a key activity and it is increasingly important to ensure that the council maximises the use of its asset portfolio in a period of reducing resources. The localism bill is likely to result in additional work and activity which promotes the transfer of assets to the third sector as a way of reducing the burden on councils e.g. through the publication of assets.

5.17 As outlined, the AMP has now been approved which sets the general direction and parameters in which asset management decisions can be taken. This was a major step forward, however the financing of the Council's aspirations for its assets e.g. Town Hall, Art Gallery & Museum and Pittville Park, as well as public realm as part of the Civic Pride proposals, has yet to be fully developed. The next development step is to supplement the AMP with a fully costed "shopping list" of aspirations for the Council's property portfolio including capital and revenue implications and the identification of options for funding. This will provide Members with a clear indication of what can be afforded from existing resources / future capital receipts and identify the potential level of prudential borrowing that may be required to fulfil these aspirations.

5.18 The Council is not yet in a position where it has enough money built into the base revenue budget to fund the annual maintenance budget (circa £1.4m) for the property portfolio. As a result, an incremental increase in revenue contribution to the Planned Maintenance Reserve used to fund building maintenance is factored into the MTFS. However, given the severity of the settlement the planned increase for 2011/12 has been deferred and the programmed maintenance for 2011/12 has been contained within the revised affordability envelope. Co-incidentally the decision to support the Everyman Theatre in their redevelopment proposals have resulted in the transfer of the maintenance liability from the Council to the theatre as a result of the move to a full repairing lease. As a one off decision this does not significantly impact on the overall strategy to increase annual contribution levels to support the annual maintenance programme but I would advise that this should not become regular practice unless the Council takes significant steps to reduce its property portfolio and maintenance liability.

5.19 The budget addressed the immediate need to top-up pump priming to support the Civic Pride Initiative in that, through the re-allocation of reserves, the Civic Pride reserve will increase to £1.1m. This will be used to support the initial works to bring sites to market, pump prime public realm improvements, plus fund the delivery vehicle.

5.20 The Prudential code allows councils to undertake non-supported borrowing to meet its objectives if this is considered to be prudent and affordable. Although a potential option, it is difficult to see how prudential borrowing can be considered at this stage given the squeeze on public finances.

5.21 The budget includes prudential borrowing from the Public Works Loans Board to fund the investment in the Runway Safety Project for Gloucestershire airport and restoration works to the Everyman theatre.

5.22 In line with the decision made by the council in October 2010 the council will, along with Gloucester City Council borrow £1.2m from the Public Works Loans Board for onward lending to the airport and to provide a temporary borrowing facility of up to £350k to carry out the runway safety works. The borrowing is to be repaid by the airport company and, as such, there is no cost to the council tax payer.

5.23 The Everyman Theatre funding proposal involves £1m of prudential borrowing from the Public Works Loans Board for onward lending to the theatre to fund the refurbishment works. The development of the funding mechanism and signing off of the business plan was delegated by Council in February 2010 the Section 151 Officer. As such, following the renegotiation of the lease, agreement of a funding agreement and finalisation of the business case, I have signed off the necessary paperwork to enable the theatre to now progress the scheme. The decision has been included in the Cabinet papers for 8th February 2011 and concludes that the business case is robust enough to ensure that the Everyman Theatre can repay the loan so that there is no cost to the council tax payer. As such, the budget includes the necessary prudential borrowing to facilitate the loan.

5.24 The Cabinet is committed to completing the AG&M subject to a bid to the HLF for complementary funding being successful and a robust business plan for future operations. The Council is being asked to underwrite the funding shortfall for the project, currently estimated at £922k. Should this materialise, the Council may need to re-assess existing funding streams, use of any future capital receipts or the potential for prudential borrowing. In considering the funding mechanism for any underwriting, the Council needs to evaluate the alternative use of any future capital receipts i.e. the potential to make treasury management decisions (such as repayment of debt premiums), which could help address the projected funding gaps by reducing cost of premium write-off in the revenue budget and avoid future cuts in services. Given the MTFS projections it is difficult see how the council could fund the cost of prudential borrowing unless the business plan for a new building, the outcome of a commissioning exercise for leisure or cuts elsewhere generated enough savings to finance the costs of financing borrowing.

5.25 The assumptions for financing the capital programme and the planned maintenance programme in the 2011/12 budget are reasonable. In moving forward, the Council must continue to ensure that it maximises the use of, and minimises the cost of, its asset portfolio.

6. Assessment of Reserves

6.1 The requirement for financial reserves is acknowledged in statute. Section 32 and 43 of the Local Government Finance Act 1992 requires billing authorities to have regard to the level of reserves needed for meeting estimated future expenditure when calculating the budget requirement.

6.2 It is the responsibility of the local authority and its Section 151 Officer to maintain a sound financial position. External auditors also have a key responsibility in reviewing the arrangements in place and may, in the course of their duties, form an opinion on the level of reserves taking into account their local knowledge of the authority's financial performance over a period of time. However, it is not the responsibility of auditors to prescribe the optimum or minimum level of reserves for individual authorities.

6.3 Within the existing statutory and regulatory framework it is the responsibility of the Section 151 Officer to advise the authority on its level of reserves. Councillors, on the advice of the Section 151 Officer, should make their own judgements on such matters taking into account all the relevant local circumstances. The adequacy of reserves can only be assessed at a local level and requires a considerable degree of professional judgement. The assessment needs to be made in the context of the authority's MTFS, its wider financial management, and other associated risks over the lifetime of the plan. The Secretary of State has reserved powers to set a minimum level of reserves to be held by councils if required.

6.4 The final budget proposals include a schedule of the reserves held by the Council, stating their purpose together with actual and proposed changes between years. These are reviewed on a regular basis and have been again in the process of finalising the budget proposals.

6.5 The MTFS provides longer term projections of reserves indicating a gradual reduction in the level of reserves over the next 5 years. This reflects the use of some of the one off reserves which are currently set aside to fund specific spending plans e.g. pensions, Art Gallery and Museum development and capital and maintenance programmes. Over this period the annual revenue budget to fund the 20 year maintenance programme will increase to around £1.4m per annum which will be more in line with the annual spend, mitigating the reduction in the maintenance reserve currently used to finance the programme. At the end of the 5 year period of the MTFS, the total level of reserves, including the General Reserve, is estimated to be circa £5.2m 2015/16. The Council may, of course build up additional earmarked reserves to meet future spending plans which are not currently identified.

6.6 Nationally the Secretary of State for Communities and Local government, Eric Pickles, is advocating that councils use reserves to support budget setting. Aside from the General Reserve, the reserves held by the council are held for specific purposes. Historically, as Section 151 Officer I have argued maintained that using reserves in this way is not a sustainable approach and, despite the suggestion, have not changed my view.

6.7 In assessing the level of the General Reserve, the Council has historically placed reliance on the degree and protection provided by earmarked reserves. Clearly there is an opportunity cost to holding reserves and I undertake a regular review to ensure that the Council does not hold money in reserves unnecessarily. This has resulted in a reduction in the number of specifically earmarked reserves over recent years. This had the potential to increase the risk of having to use the General Reserve but, in practice, has not caused an issue and is therefore a reasonable strategy. Money held in reserve ties up resources which could be spent on one off initiatives. However, conversely, every £100,000 held in reserve earns approximately £500 for the Council which is budgeted for in the revenue estimates as treasury management income.

6.8 The Council has previously agreed to aim to maintain its General Reserve at approximately 10% of net operating expenditure, or a level between £1.5m and £2m. The budget proposals for 2011/12 include the re-alignment of reserves to maintain the size of the General Reserve at c£2m. Although the Council has managed to deliver services without calling in the General Reserve, there is a potential for it to be called upon given the considerable period of change resulting from the need to drive out savings and the potential to need to support the commissioning programme of activity with one off money. There are other pressures which are to be considered in a confidential report to council which may put further pressure on the General Reserve. In addition, although measures are in place to address the projected overspend 2010/11, the year has yet to conclude and the outturn yet to confirm that the strategy has worked without needing to call on the General Reserve.

6.9 The delivery of the budget for 2011/12 and many of the Bridging the Gap initiatives which support it, has required 'up front' investment. The revenue budget is now extremely tight and there is less potential to deliver underspends, particularly in the current economic climate. In order to continue to deliver future savings as quickly as possible, it is important to have access to one off money. Therefore, I would recommend that Members take every opportunity to use further one off windfalls i.e. either future budget underspends or windfall funding, to top up the General Reserve. My advice would be that the level of General Reserve should be maintained toward the top end of the range £1.5m - £2m to fund future up front investment costs.

6.10 The triennial revaluation of the pension fund in 2010 resulted in an increase in the contribution rate. Historically the impact of the increase has been managed and phased in through the use of the pension reserve, which is now exhausted. However, given that the budget allows for the increasing in contribution rates within the base budget, no top up of the pension reserve is required.

6.11 **Overall, I am satisfied that the projected levels of reserves are adequate for the forthcoming year and that the balance of reserves held is about right. However, there are still some uncertainties over the duration of the MTFS, particularly in respect of funding the aspirations for the Council's property portfolio.**

7. Budget setting and monitoring.

7.1 In response to the reduction in public spending, the Council supported the budget consultation exercise which was undertaken over the summer of 2010. Whilst not perfect, this proved to be a valuable exercise with both positive feedback from Members, officers, residents and the local media. It provided some important indicators to the Cabinet as to where to look in making their decision for 2011/12 budget. Looking ahead, Members need to consider how it can build on this work to inform decisions in respect of outcomes to be commissioned by the Council in future.

7.2 The Council has a good track record in budget setting and financial management which is recognised by the council's auditors. It has a history of delivering services within budget and has a regular budget monitoring process which is reported to Cabinet and ensures that corrective action can be taken to address any in year financial issues where appropriate, as was the case in the current year 2010/11.

7.3 The Council has end of year procedures in place for budget under/overspends which are actively designed and communicated to ensure openness and positive financial management in removing the temptation to spend unnecessarily at the year end in order to use up unspent budgets.

7.4 Sound financial management is key to the success of the organisation and Officers continue to look at ways of improving financial management information. Training in both the use of the system and in budgetary control takes place on an on-going basis.

8. Corporate Risk Management

8.1 The Council's work around risk management continues to develop. Divisions and project and programme managers regularly review their individual risk registers and continue to improve procedures / take action to mitigate risk where possible. The Council's corporate risk register is now assessed monthly by SLT and reported quarterly to Cabinet.

8.2 Whilst the Council has made some progress in tackling some of the key risks or recognises the need to undertake work in the near future to deal with others, it continues to be challenged by the issue of capacity. The Senior Leadership Team are tackling capacity issues through the development of resource planning with a view to focusing scare resource and money into high priority work.

8.3 The Council provides a wide range of services which should be re-examined in the light of reducing resources. The Council's decision to become a commissioning authority will help to focus the Council on outcomes for the residents given the financial outlook.

8.4 The budget proposes a reduction in the level of staff training which has the potential to impact on staff professional capability. However, given increased sharing of services and expertise and new methods of training e.g. e-learning this does not propose an impact on corporate governance arrangement. However, in considering the budget proposals, the Audit committee were concerned that project management training remained a high priority despite the proposed cuts in training budgets.

8.5 **I am satisfied that the budget, as far as is possible within limited resources, aims to tackle some of the key risks in the corporate risk register and poses no significant increase in risks.**

9. Conclusions

9.1 The Local Government Act 2003 requires the Section 151 Officer to report to Council on the robustness of the budget estimates and the adequacy of reserves. This report aims to address this requirement and draws together a number of challenges and issues that are likely to face the Council in future years. The key issues and messages which require Members consideration in approving the budget proposals for 2011/12 include the following:

- The impact on the Council's funding levels as a result of the Governments response to the management of the level of national debt.

- The impact of the recession on income levels for services and investment income levels resulting from sustained low interest rates.

- The measures to deal with the exposure to Icelandic banks built into future financial projections.

- The funding implications of the AMP and future capital and maintenance programmes for Council owned assets.

- The capacity required to deliver the 'BtG' programme work streams for closing the funding gaps.

- The need to develop cross party working in light of the public sector funding squeeze in order to seek buy-in to more difficult decisions.

- The need to maintain the reserve levels to fund future 'one-off' costs given the pressure on the General Fund budget.

- The overall financial standing of the Council, despite the challenges ahead, is currently sound.

- The Council has a reasonable level of reserves.

9.2 Members are asked to consider the advice provided in this report, in line with statutory duties placed on Members, based upon my assessment of the robustness of the overall budget and estimates in the Medium Term Financial Strategy.

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Appendices	None
Background information	1. Final budget proposals 2011/12