Finance and Resources Committee

10.00am, Thursday, 14 January 2016

Council's Budget 2016/20 – Risks and Reserves

Item number	7.7
Report number	
Executive/routine	
Wards	

Executive summary

The report advises members on the risks inherent in the revenue and capital budget framework and the range of measures and provisions established to mitigate these.

Links

Coalition pledges	P30
Council outcomes	CO25
Single Outcome Agreement	**SO1**, **SO2**, **SO3**, **SO4**

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Report

Council's Budget 2016/20 – Risks and Reserves

Recommendations

1.1 Members of the Finance and Resources Committee are asked to:

1.1.1 note the content of this report; and

1.1.2 remit the report to Council for decision on 21 January 2016 as part of the budget setting process.

Background

2.1 This report advises members of significant risks identified in the budget process, quantifying these wherever possible, and sets out the range of measures and provisions put in place to mitigate these.

2.2 General or unallocated reserves are held against the risk of unanticipated expenditure or reduced income arising in any particular year. In addition some specific/earmarked reserves are set aside to manage timing differences between the receipt of income and expenditure being incurred, in accordance with accounting rules.

2.3 The reserves held by the Council are reviewed annually as part of the revenue budget process. The review considers the level of balances, the risks inherent in the budget process and the adequacy of arrangements in place to manage these known risks.

Main report

Risks

3.1 There will always be risks inherent in the budget process. What is important is that these are identified and mitigated / managed effectively. Appendix 1 shows a risk matrix, setting out how the known risks identified in this report are managed. It is important to recognise, however, this list should not be seen as exhaustive due to the complexity of the Council's activities and the environment within which it operates.

3.2 Risks have been categories into one of three groups – (i) risks associated with the delivery of major projects, savings proposals, internal improvement plans and severance costs, (ii) on-going risks and (iii) emerging risks. The most significant of these are summarised below:

Risks associated with the delivery of major projects, savings proposals, internal improvement plans and severance costs

3.3 The budget process makes assumptions about the delivery of major projects and the level of savings that can be achieved. There are a number of potential risks within this area:

- The ability to deliver both the savings already approved by Council that impact in 2016/17 and savings proposals set out in the revenue budget framework for decision on 21 January 2016, within the timescales stated; and

- The deliverability of services within the baseline level of available resources, particularly in areas where the majority of expenditure is demand-led in nature.

3.4 The budget proposals set out at the Finance and Resources Committee meetings on 24 September and 26 November 2015 are sufficient to address the Council's net savings requirement up to and including 2018/19, if all are accepted. Inbuilt to these proposals are additional savings which provide the potential for an element of the proposals not to be taken forward.

3.5 A robust process of active tracking and reporting on savings delivery has been established during 2015/16. Progress will continue to be regularly reported to the Finance and Resources and relevant Executive Committees in conjunction with ongoing budget challenge meetings by service directors.

3.6 The Transformation programme will impact on overall employee numbers and there will be significant staff release costs associated with this. It is not possible to assess the adequacy of provisions with certainty at this stage as the work-streams are not at an advanced enough stage to quantify the timing and magnitude of the total funding requirement.

On-going risks

3.7 The ICT Transformation programme has funding set aside for additional investment to support the transition to the new provider. There is sufficient funding for currently known commitments however there are risks around additional costs arising as the migration process moves forward.

Financial Settlements and wider fiscal policy changes

3.8 Details of the 2016/17 financial settlement were announced on 16 December 2015 and confirm a reduction of funding of £16.7m compared to that assumed in the budget framework, details of which are oultined in the Budget Update report elsewhere on today's agenda. Whilst plans for 2016/17 reflect the confirmed level of funding, the levels of funding for future years could vary for a number of reasons, including updated population data and the complexities of the distribution formula. Implementation of the principal recommendations contained within the Scotland Bill 2015-16 could also have a significant impact on the future funding arrangements for national and local government. While based on best-available assumptions, levels of public expenditure are furthermore subject to both Scottish Government and wider UK Government fiscal policy.

Loss of income

3.9 Assumptions are made in the budget process on the level of income that will be generated for services. There are risks related to these assumptions around (i) demand for chargeable services and (ii) the ability to collect all income due. The Council has a range of measures to mitigate the risk, such as service level agreements with external users, application of the Council's corporate debt policy and regular monitoring.

Demographic changes

3.10 The risk relates to the overall level of demand for services and the ability to provide for this within the available resources. The budget framework identifies £12.1m in 2016/17 for additional expenditure due to demographic pressures, reflecting the additional £2.1m approved in June 2015 to acknowledge the net impact of higher numbers of school pupils, those with learning and/or physical disabilities and at-risk children than previously projected.

3.11 The review of the current level of provision within the Long Term Financial Plan reported to Committee in June identified additional potential cumulative pressures within Children and Families services of £7m over the period from 2017/18 to 2019/20 and there is a risk that the current level of provision may not be sufficient to meet the actual cost pressures.

Council Tax Freeze

3.12 The budget framework assumes that 2016/17 will be the last year of the Council Tax Freeze, in line with the Scottish Government's policy commitment over the current parliamentary term. An additional £7m of income is included in the framework as a result of levying an indicative 3% increase in 2017/18 and each year thereafter. There is a risk that this increase is not achieved and alternative income or compensating savings are required. More fundamentally, there is a risk that changes to the system of local taxation result in a lower-than-anticipated overall level of revenues generated, although this seems less likely due to a broad consensus around making current arrangements more progressive.

Infrastructure

3.13 The risk relates to there being insufficient resources to maintain adequately the Council's existing and planned infrastructure, resulting in reduced service provision and / or increased costs in the future. Members of the Corporate Leadership Team (CLT) have considered where any additional service investment within the budget framework might be best directed and, at this stage, identified property repairs and maintenance as the key priority.

Local Development Plan

3.14 There is a significant risk that the Council will require to support additional borrowing and running costs associated with new infrastructure required as a result of the Local Development Plan. No specific revenue provision is included at this stage pending greater certainty over the financial impact and profile of this requirement.

Large-scale emergencies

3.15 The risk relates to the Council requiring to meet the first £1.896m (2015/16 threshold) of any costs for large-scale emergencies for which claims are made under the Bellwin scheme and the ability to manage this within the overall level of resources available to the Council. Bellwin thresholds represent 0.2% of a local authority's budgeted net revenue expenditure.

Statutory notices

3.16 Provisions have been made within the financial statements to 31 March 2015 for impairment of the debtors balance relating to statutory notices and settlements. The current provisions are deemed to be sufficient however there is a potential risk of failure to recover expected amounts of outstanding debts. The detailed position on billing and recovery is reported on a monthly basis to the Finance and Resources Committee.

Universal Credit / Welfare Reform

3.17 The risk relates to the impact on service and Housing Benefits budgets from the introduction of Universal Credit as it is rolled out across Scotland. Welfare reform will provide further exposure to risk through, for example, non-direct deductions for Council Tax Reduction elements of Council Tax bills.

3.18 There are risks that service users will suffer financial hardship which may impact on housing, health and general welfare resulting in greater need for emergency intervention from Council services.

Dilapidations and other related contractual commitments

3.19 Dilapidation costs relate to payments for disrepair at the termination of leases. A reserve has been established for dilapidations however there is a risk that the sums within this will not be sufficient. There are ongoing negotiations related to a number of properties; the value and timing of these settlements is as yet unknown.

Legal Claims

3.20 There is an increased risk of compensation claims arising as a result of specific events and emerging issues.

Inflation

3.21 The majority of the Council's operating expenditure, whether incurred directly or indirectly (including employee costs), is subject to the effects of inflation. Corresponding provision has therefore been made across all key areas of expenditure, based on available economic forecasts and other relevant factors. Particularly in the case of contractually-committed sums and negotiated settlements, however, there is a risk that this level of provision is insufficient.

3.22 An increase in interest rates could also impact on borrowing costs. The Treasury team, however, monitors the position to mitigate the impact on the Council.

Health and Social Care Integration

3.23 There is a risk that funding will be insufficient to deliver the planned outcomes. The Integration Joint Board has been established and work is ongoing to identify how the available resources are to be spent to deliver on the national outcomes and how the balance of care will be shifted from institutional to community-based settings within available resources. The volatility of expenditure in areas of the National Health Service may expose the Integrated Joint Board to further financial risks.

Capital Receipts

3.24 There is a risk relating to the realisation of capital receipts in line with amounts assumed in the capital investment programme and the ability to afford and deliver the full programme if these do not materialise, together with assumed contributions to both the Strategic Acquisition Fund and staff release costs associated with the transformation programme.

Emerging risks

City Region Deal

3.25 The Council may incur additional borrowing costs or require short-term cash flow funding in supporting its participation in the City Region Deal for the Edinburgh and South East of Scotland Region. No specific provision is included at this stage, pending greater certainty over the financial impact and profile of this requirement.

National Minimum Wage

3.26 The Chancellor of the Exchequer announced in July 2015 a staged increase in the level of the national minimum wage to around £9 per hour by April 2020 based on median earning projections. While the direct impact on the Council is not anticipated to be significant given the current payment of the Living Wage of £7.85 per hour, the annual financial impact in the area of purchased care (where average pay rates are currently below this level) could potentially exceed current levels of provision by around £9m by 2019/20.

Tram extension

3.27 The report to Council on 19 November 2015 provided an update on the proposed Edinburgh Tram extension, including the route of the extension and the potential financial implications.

Apprenticeship Levy

3.28 The Chancellor's Spending Review and Autumn Statement on 26 November 2015 confirmed the introduction of an Apprenticeship Levy of 0.5% of an employer's pay bill, applicable to large employers (over 250 employees), to be implemented by 1 April 2017. While the levy will apply to all UK employers, precise arrangements for implementation are devolved to the Scottish Government.

Reserves

3.29 Members are aware that the Council holds a number of earmarked balances within the General Fund. At 31 March 2015, the General Fund balance stood at £117.476m, of which £104.451m was earmarked for specific purposes. The unallocated General Fund balance remained at £13.025m, in line with the medium term strategy. There are planned movements in reserves during 2015/16, with a projected balance at 31 March 2016 of £106.367m.

3.30 The current budget does not provide for any further contributions to the unallocated General Fund. The level of reserve at 31 March 2015, together with the forward strategy, is considered appropriate in light of the financial risks that are likely to face the Council in the short to medium term.

3.31 There are a number of planned contributions to / from the earmarked balances held within the General Fund. Details of these planned movements are shown in Appendix 2. Appendix 3 provides details on the purposes of the main earmarked balances held.

3.32 The amount held in the insurance fund is deemed adequate, taking into consideration the estimated value of outstanding claims. This is subject to on-going review.

3.33 The Capital Fund has been built up over a number of years, the level of reserve as at 31 March 2015 stood at £35.927m. Members are reminded of the approval to draw down £7.5m of funding from this reserve to support capital investment priorities during 2015/16, with retained reserves of £28.427m projected at 31 March 2016.

3.34 There will be a call on a number of the earmarked reserves, including the Capital Fund, to support the funding of staff release costs of the Transformation Programme. The timing and value of this call on reserves has yet to be fully established and will be reported to Committee as the programme progresses.

Measures of success

4.1 The Council identifies and quantifies, where possible, risks that are inherent in the revenue budget in advance of these materialising and puts mitigating actions in place.

4.2 The Council maintains an adequate level of unallocated General Fund reserves.

Financial impact

5.1 The report identifies where funding has been made available for the risks set out. Council holds unallocated General Fund reserves against the likelihood of unfunded risks occurring.

Risk, policy, compliance and governance impact

6.1 The aim of this report is to identify the key risks to the Council and outline actions to manage those risks through planning, mitigating actions and use of reserves, as outlined in the attached appendices.

Equalities impact

7.1 While there is no direct additional impact of the report's contents, all budget proposals are now subject to an assessment of their potential equalities and rights impacts. The equalities and rights impacts of any substitute measures identified to address savings shortfalls are similarly assessed.

Sustainability impact

8.1 While there is no direct additional impact of the report's contents, the Council's revenue budget includes expenditure impacting upon carbon, adaptation to climate change and contributing to sustainable development. In addition, all budget proposals are now subject to an upfront Impact Assessment.

Consultation and engagement

9.1 A budget consultation and engagement exercise has been undertaken.

Background reading/external references

Council's Budget 2015/16 - _Risks_and_Reserves, City of Edinburgh Council, 12 February 2015

2016_20_Revenue_and_Capital_Budget_Framework, Finance and Resources Committee, 24 September 2015

2016_20_Revenue_and_Capital_Budget_Framework, Finance and Resources Committee, 26 November 2015

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Links

Coalition pledges	P30 – Continue to maintain a sound financial position including long term financial planning
Council outcomes	CO25 – The Council has efficient and effective services that deliver on objectives
Single Outcome Agreement	SO1 – Edinburgh's economy delivers increased investment, jobs and opportunities for all SO2 – Edinburgh's citizens experience improved health and wellbeing, with reduced inequalities in health SO3 – Edinburgh's children and young people enjoy their childhood and fulfil their potential SO4 – Edinburgh's communities are safer and have improved physical and social fabric
Appendices	Appendix 1 – Risk Matrix Appendix 2 – Projected Movement in General Fund Appendix 3 – Earmarked balances

Appendix 1

Risk Matrix

The table below summarises how the risks identified in the report are managed. Explanations of the actions set out in the "Provision to Manage" column follow the table.

Risk	Provision to Manage
Transformation programme	Workforce Reductions – Earmarked provision
	Regular monitoring of savings delivery
Financial settlements	Long-Term Financial Plan
	Regular monitoring of public expenditure projections and recognise potential or actual grant variations in LTFP
Demographic changes leading to rising service demands	Long-Term Financial Plan
Infrastructure	Asset Management Plan / Mitigating Action
Large scale emergencies	Unallocated reserve
Property conservation	Earmarked provision / Unallocated reserve
Dilapidations	Long-Term Financial Plan
Legal Claims	Unallocated reserve
Service area -specific risks	Mitigating action
Universal Credit/Welfare Reform	Long-Term Financial Plan Ongoing monitoring of impacts
Health and Social Care Integration	Ongoing development of Strategic Plan with NHS

Definitions of 'Provision to Manage' used in above table

Asset Management Plans – will require to be addressed through asset management plans.

Earmarked provision – the Council has set monies aside in an earmarked reserve or other provision to meet the estimated costs.

Mitigating Action – Directors to identify alternative measures to manage risks within available resources

Long-Term Financial Plan – provision in the Long-Term Financial Plan

Unallocated Reserve – Council would require drawing funding down from the unallocated General Fund balance to meet costs

Projected Movement in General Fund

Appendix 2

	Projected Balance at 31.3.16 £000	Projected Investment / (Withdrawal) £000	Projected Balance at 31.3.17 £000
Unallocated General Fund	13,025	-	13,025
Balances Set Aside to Manage Financial Risks			
Balances Set Aside For Specific Investment	8,936	(3,560)	5,376
Council Priorities Fund	66	1,700	1,766
Contingency Funding, Workforce Management	12,901	(10,002)	2,899
Dilapidations Fund	9,476	(1,500)	7,976
Insurance Fund	12,605	48	12,653
Balances Set Aside from Income Received in Advance			
Licensing Income	1,405	4	1,409
Lothian Buses	5,000	(3,000)	2,000
Other Minor Funds	234	(40)	194
Pre-paid PPP Monies	1,599	135	1,734
National Performance Centre	1,996	(1,996)	0
Council Tax Discount Fund	20,907	(1,316)	19,591
Unspent Grants	4,180	0	4,180
Strategic Acquisition Fund	7,500	(2,000)	5,500
Balances Set Aside for Investment in Specific Projects which will Generate Future Savings			
IT Transformation	782	(782)	0
Energy Efficiency	863	3	866
Spend to Save	3,892	(1,411)	2,481
Balances Set Aside under Devolved School Management Scheme			
Devolved School Management	1,000	0	1,000
Total General Reserve	**106,367**	**(23,717)**	**82,650**
Capital Fund	**28,427**	**(28,427)**	**0**

Earmarked balances

Appendix 3

Balances set aside to manage financial risk	**Source/purpose**
Balances set aside for specific investment	Funding set aside for specific projects; including improveIt and iPFM.
Council Priorities Fund	Monies set aside primarily from service and corporate underspends, combined with the residual balance from the former budgetary flexibility scheme, which are utilised to meet key Council priorities or expenditure pressures
Contingency funding, Workforce management	Held to cover costs of workforce management changes including staff severance costs.
Dilapidations Fund	This represents monies set aside to meet dilapidation costs arising from the termination of property leases and other related contractual commitments.
Insurance Fund	Insurance Funds can be used to defray any loss where an authority could have insured against a loss but has not done so and for paying premiums on an insurance policy. This includes the power to meet excesses on insurance policies.
Balances set aside from income received in advance	
Licensing Income	This represents the surplus derived from licensing cabs and houses in multiple occupation and liquor licences. Council is not permitted to use this surplus on other services.
Lothian Buses	Holds dividend income previously paid by Lothian Buses which will be drawn down to support operations of Transport for Edinburgh.
Other Minor Funds	Minor funds held in respect of major exhibitions, social inclusion and a legacy for Craiglockhart Young People's Centre
Pre-paid PPP monies	Holds monies set aside in recognition of the phasing issues relating to the former 'level playing field support' grant monies.

Balances set aside from income received in advance (cont.)	**Source/Purpose**

National Performance Centre	Holds monies returned by the police and fire authorities at March 2013, following the creation of unitary providers. Proposed to use as the Council's contribution for the National Performance Centre for Sport.
Council Tax Discount Fund	Holds monies received as a result of reducing Council Tax second home discounts. Use of the fund is prescribed by the Scottish Government and is restricted to affordable housing type projects.
Unspent grants	Holds monies set aside at the year end, in accordance with proper accounting practice, where income has been received prior to the relevant expenditure being incurred.
Strategic Acquisition Fund	Funds set aside to sit alongside private sector finance to create new city development opportunities.

Spend to Save

IT transformation	Monies set aside from efficiencies in the ICT contracts for the following purposes: (i) cash releasing efficiency projects; (ii) modernising government, through enhanced use of IT; (iii) new ways of working; and (iv) strategic financial planning
Energy Efficiency	Monies received from the Scottish Government's Energy Efficiency Initiative to facilitate the operation of spend-to-save schemes in this area. While this fund will cease to be ring-fenced with effect from April 2016, it is the expectation that monies will continue to be invested in energy efficiency-related measures.
Spend to Save	A fund set up in February 2000 to assist service areas to deliver revenue savings in future years through longer-term financial planning.