

# Report of the Director of Finance to the meeting of Executive to be held on 24 February 2015 and Council to be held on 26 February 2015.

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## Subject:

S151 Officer's assessment of the robustness of the proposed budget estimates for 2015/16, and of the adequacy of forecast financial reserves

## Summary statement:

This report assesses the risks related to the proposed budget for the financial year 2015/16, and the adequacy of the available mitigations, in the context of the forecast reserves. It concludes that the estimates are sufficiently robust to allow the Council to set the budget, but raises concerns about the adequacy of reserves after 2016/17 unless further action is taken during the 2015 planning round.

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**Overview & Scrutiny Area: N/A**



## **1. SUMMARY**

This report assesses the risks related to the proposed budget for 2015/16, and the adequacy of the available mitigations. The budget proposed is for one year only, but the assessment is made in the context of the proposed reserves and the outlook to 2017/18.

The report concludes that the estimates as proposed are sufficiently robust to allow the Council to set the budget.

£12.6m of the Unallocated Corporate Reserves set aside to support the revenue budget are drawn down to provide a balanced budget in 2015/16. For 2016/17, a further drawdown from reserves of £7.6m is planned. At that point, they reach £12.6m, and a budget deficit remains, of £11.8m. The deficit is £51.9m for 2017/18. This class of reserves can cushion less and less the impact of the deficit. Accordingly, continued and deep reductions in the net cost of Council services will be required, which must be planned during 2015.

## **2. BACKGROUND**

I am the Council's S151 Officer under the Local Government Act 1972. Under Section 25 of the Local Government Act 2003, when the Council sets the budget, I am required to report on:

- the robustness of the estimates made for the purposes of the calculations, and
- the adequacy of the proposed financial reserves.

This report comments on the revenue and capital estimates in the proposed budget. My assessment is informed by extensive personal involvement in the development of the proposed budget.

## **3. OPTIONS**

This report does not set out alternative options. Legislation requires Council to have regard to this report and my assessment when setting the budget.

## **4. FINANCIAL & RESOURCE APPRAISAL**

The financial appraisal underpinning my assessment is set out in the separate budget reports to this Executive.

My assessment is as follows:

- the financial outlook remains very challenging, with national public finance policy for the foreseeable future likely to place the local authority sector under continued funding squeezes

- the outlook may be affected by Government fiscal policy, after the 2015 General Election, on the level of total UK public expenditure and the share flowing through local government. There may also be national decisions on the future of health and social care. For now, this assessment is based on the direction of UK finance policy indicated by the current Government's stance, and reflects existing health and social care policy
- the principal financial imperative for the Council is to reduce its recurrent cost base, in order to remain a credible and viable organisation. The budget being proposed balances the 2015/16 budget, but in-year deficits remain at £11.8m for 2016/17, rising to £51.9m for 2017/18
- The scale of the changes required to deliver cost reductions mean a complex programme of change with typically 6-9 month lead times. The programme will include changes agreed by Budget Council in 2014, with a wide range of individual changes of varying magnitude, risk and timescales
- The proposed budget is for 2015/16 only, though the consequences of the proposals are forecast into later years. In the context of a projected financial outlook to 2020/21, published in its Medium Term Financial Plan, the Council is planning for the longer term through its New Deal programme. Its conclusions will need to shape future budget rounds; for now, the unclosed deficits remain
- The new amended and accelerated proposals have been developed with the Executive members, and reflect extensive engagement from Portfolio Holders, and management teams, which started in autumn 2014
- Extensive public and internal consultation has allowed the new amended and accelerated proposals to be tested, refined, and their impacts better understood
- The range of proposals to reduce net costs is wide, and distributed across the Council, which in itself diversifies the risk. In many cases the proposed changes are independent and mutually exclusive at an operational level. However, the changes for Adult and Community services are typically interdependent, and have consequences for the health economy
- Experience in 2014/15 has shown that risks to the implementation of changes in Adult and Community Services, will need very close monitoring, backed by appropriate contingency
- Savings in Adults and Community Services which can have consequences for the District-wide health and social care economy require effective collaboration with the NHS and other partners. Through their responses to the budget consultations, it is clear that NHS partners recognise that need and welcome the opportunity to participate in shared planning
- £2.9m proposed savings will derive from entitlements to and methods of transporting individuals to and from services. The scale of the proposed change and the characteristics of the people affected make implementation complex and potentially prone to delay. No specific contingency has been included in the base revenue budget.

- In 2014/15 plans to reduce waste management costs were thwarted by unexpected increases in the volume of waste produced in the District. A repetition of that trend poses a risk
- The proposed allocation of the Dedicated Schools Grant has been the subject of extensive and detailed development, scrutiny and ratification by the Schools Forum and its working groups. The proposed £1.246m Joint Improvement Investment Fund is subject to Secretary of State approval
- Lessons from financial performance in 2014/15 have been reflected in the proposed budget, through the adjustment of selected expenditure and income budgets totalling around £3m
- Adjustments to the base estimates to reflect changes in prices have been revised to reflect latest inflation data as it relates to the Council's cost base and supply chain
- In a turbulent and changing environment, there will always be a residual risk that activity will not be delivered to planned timescales. Where this occurs, mechanisms are available to carry forward funds between years. Based on previous years experience, there is a risk that around £5m of non-recurrent revenue may carry forward. This is an acceptable financial risk except where delays means failure to deliver timely savings – these need to be managed on a case by case basis
- All savings proposals are allocated to a responsible Director; there are no unallocated reductions
- Slippage of the Capital Investment Plan can be managed without risk to affordability
- Contingencies in the base revenue budget have been set at a level consistent with experience in 2014/15, being pegged at a total of £3.6m.

I confirm therefore that the estimates are sufficiently robust for the purpose of calculating the budgetary requirement.

## **Reserves**

The Council's financial strategy over the last 4 years has been to maintain the strength of the balance sheet to provide resilience in a turbulent environment, whilst reducing the recurrent net cost base. The Council adopted and has adhered to a policy on the use of reserves which has served it well.

The balance sheet includes reserves set aside for designated purposes and for specific liabilities and risks. This assessment focuses on the level of Unallocated Corporate Reserves available to support revenue budgets.

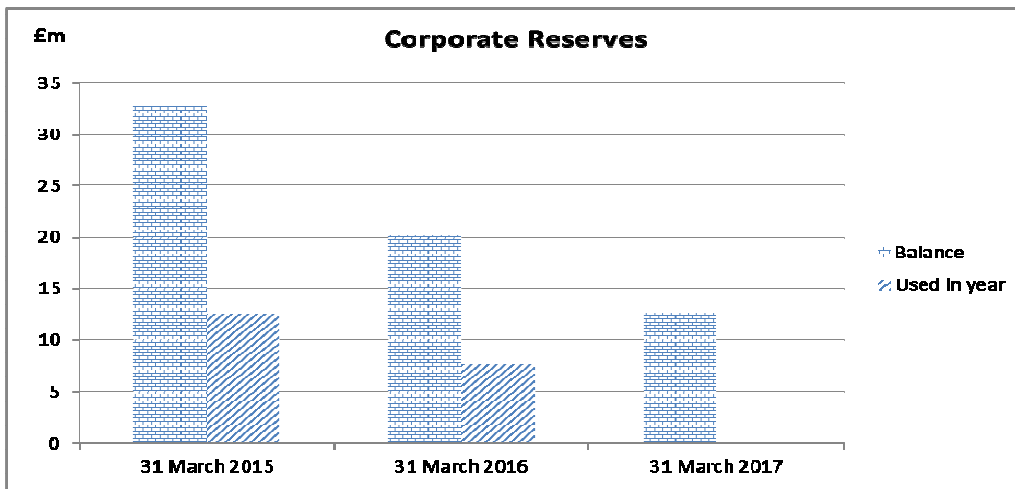
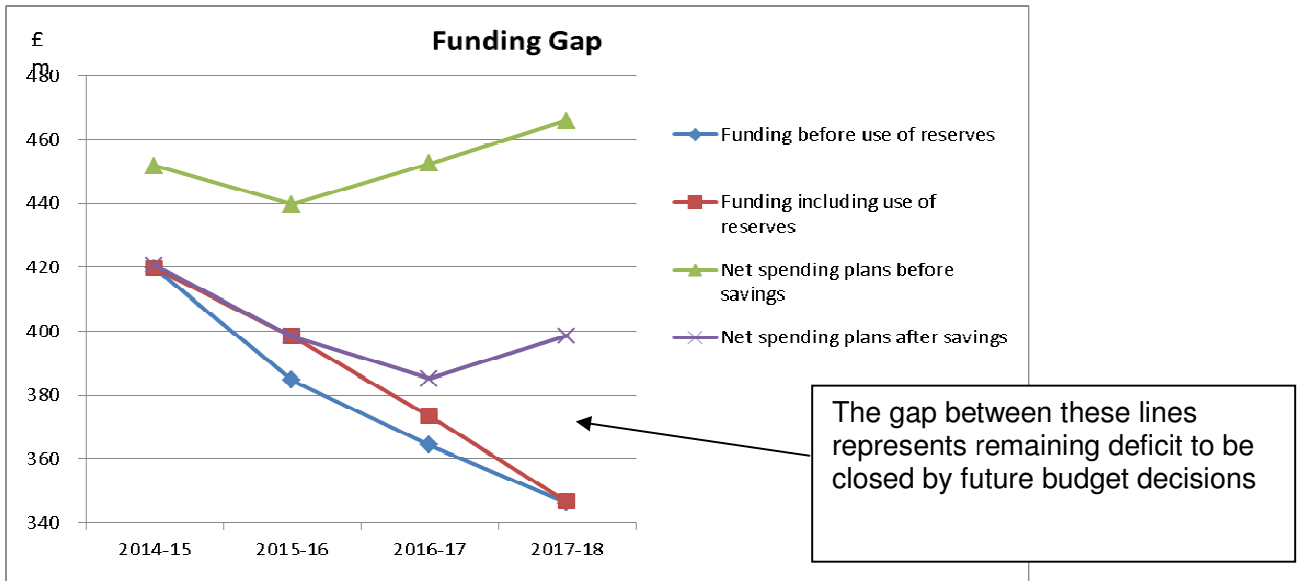
The Council has been successful in reducing its recurrent cost base since 2010/11, and has been able to augment, then deploy, Unallocated Corporate Reserves. They will stand at a forecast £32.8m at April 1 2015.

The outlook for the next three years is, on current proposals and *before* use of reserves, for a revenue deficit of £13.6m in 2015/16, £20.9m deficit in 2016/17, with a projected

deficit of £52.3m in 2017/18. The proposed Budget assumes that Unallocated Corporate reserves will be drawn down over the next two years, after which they will stand at £12.6m at the beginning of 2017/18.

The graphs below show the gaps between funding and spending which remain before and after savings and use of reserves each year, and the remaining Unallocated Corporate Reserves.

**Graph Showing Gaps Between Funding and Spending**



Appendix A of Document BF to this Executive contains details of the 3 year position, based on the proposed budget. Appendix F of that paper projects what the resultant balance on corporate reserves would be given the current proposals.

I conclude that the reserves are adequate for the 2015/16 proposed budget.

On current plans, they will be drawn on for 2016/17 (along with £1.4m of other reserves), but even then a deficit remains of £11.8m.

The position in 2017/18 is very difficult. There is in my view an unreconciled tension between resources, citizen expectations, and the statutory framework which may at least inhibit, if not prevent, the Council from curtailing or stopping entirely services. This applies particularly to services provided to individuals of all ages who, because of their personal circumstances, qualify for personal services. There are many decisions the Council can take to remain financially viable, but agreeing the cost reduction plan will be politically and managerially challenging.

In my view, projected Unallocated Corporate Reserves for 2016/17 would, on current estimates, be inadequate in the absence of further net cost reductions for the following reasons:

- This class of reserves can cushion less and less the impact of the revenue budget deficit
- There remain significant risks to the delivery of the proposed service savings
- The amount of contingency in the base budget has already been stripped back
- Having very constrained reserves provides limited resource to finance non-recurrent invest-to-save or transformational activity
- A residual general reserve of c £12m represents 3% of the affordable projected net revenue spend of £347m in 2017/18 in what will remain a highly turbulent environment, given the continuing difficult outlook for public finances. Aiming for Unallocated Corporate Reserves in the range of £12-15m would, in my view, retain the resilience of the Council's position.

I therefore conclude that:

- while the proposed budget leaves an adequate level of reserves for 2015/16, the closing position for 2015/16 depends on continuous management of implementation risk
- for 2016/17 and beyond, it is imperative that the Council agrees further reductions to net revenue expenditure, aiming for a balanced in-year revenue budget in that year. The planning and consultation for the future has already started, through the New Deal programme, and budget proposals for 2016/17 and beyond need to be well advanced by autumn 2015
- Elected Members, citizens and service users, and our partners should be prepared for the need to accept further changes in the scale and cost of Council activity, at the latest during 2016/17, over and above the proposed budget.

## **5. RISK MANAGEMENT AND GOVERNANCE ISSUES**

In reaching this conclusion I have modelled the potential financial impact of the risks identified in Appendix 1 to this paper. Using a quantitative method combining the likelihood and impact of adverse events occurring, I estimate that the level of risk that needs to be managed is in the order of £9m to avoid further calls on the corporate reserves. This risk analysis will be used to inform management action during the year.

The existing and proposed governance mechanisms to manage the budget are examined as part of my risk assessment.

## **6. LEGAL APPRAISAL**

This assessment is made in accordance with the requirements of the Local Government Acts 1972 and 2003. The Council's Constitution provides that each year, before the budget is determined the Director of Finance will produce a report for the Executive showing ongoing commitments and a forecast of the total resources available to the Council to enable the Executive to determine any financial strategy guidelines.

## **7. OTHER IMPLICATIONS**

The Equality and Diversity issues arising from the amended, accelerated and new budget proposals are analysed in the reports accompanying the budget documentation presented to Executive on 10 February and 24 February 2015. The Interim Trade Union feedback on the amended, accelerated and new budget proposals was detailed in a separate report presented to the meeting of Executive on 10 February 2015 (Document AZ). The Trade Union feedback and the feedback from the public engagement and consultation programme on the proposals previously approved by Budget Council in February 2014 was fully considered by Council at that time.

## **8. RECOMMENDATIONS**

That Members have regard to this report in setting the budget, and in particular note my conclusions that:

- the estimates presented to Council are sufficiently robust for the purpose of calculating the budgetary requirement
- the reserves are adequate for the 2015/16 proposed budget, and will be drawn on in accordance with reserves policy, recognising that estimates will be subject to review as part of the rolling planning cycle
- the projected 2016/17 corporate reserves balance would, on current estimates, be inadequate, unless further cost reductions are planned during 2015, aiming for a balanced in-year revenue budget for 2016/17 and beyond.

## **9. APPENDICES**

**Appendix 1:** Risk-Based Assessment of Potential Events

## **10. BACKGROUND DOCUMENTS**

- 2015-16 Budget and financial outlook to 2017 – Executive Report 2<sup>nd</sup> December 2014 (Document AD)
- 2015-16 Budget Update – Executive Report 10<sup>th</sup> February 2015 (Document AX)
- Engagement and Consultation Programme in relation to amended,

accelerated and new budget proposals for the 2015/2016 Council budget – Executive Report 10<sup>th</sup> February 2015 (Document AY)

- Interim Trade Union feedback on the Council's amended, accelerated and new budget proposals for the 2015/2016 Council budget – Executive Report 10<sup>th</sup> February 2015 (Document AZ)
- The Council's Revenue Estimates for 2015-16 – Executive Report 24<sup>th</sup> February 2015 (Document BF)
- The Council's Capital Investment Plan for 2015-16 onwards – Executive Report 24<sup>th</sup> February 2015 (Document BG)
- Allocation of the Schools Budget 2015/16 Financial Year – Executive Report 24<sup>th</sup> February 2015 (Document BH)



### Risk-Based Assessment of Potential Events Affecting the Proposed 2015/16 Budget and Beyond

The table outlines: the risk event that could occur and cause the plan to vary; the mitigations that are in place; and an assessment of the potential quantified impact of the individual risk materialising, together with the additional mitigating factors.

Risk Event	Description and Mitigation in Place	Residual Risk Rating (Likelihood/Impact) and Contingency
		Likelihood: Low <30% <Medium < 70%< High Impact: Low <£2m< Medium < 5m < High
Government funding reduces further than forecast	Although the 2015/16 funding settlement has been announced, it is possible that a post-election Spending Review could affect 2015/16. Monitoring in place of key fiscal cycle events for 2016/17. Public finance in next Parliament likely to mean continued austerity, but specific impacts on Bradford not certain. Planning arrangements in place allow lead time for future budget plans to be flexed for future years	Medium/low  Contingency provided through balance sheet reserves for 2015/16  Contingency provided through adjustment of plans for subsequent years
Taxation streams are unstable	Collection rates and bad debt provision have been revised in the light of actual experience of the Council Tax Reduction scheme, Business Rates appeals and relief regime Tax base yields are better understood now recent reforms have bedded in. Business Rates regime and performance has been more volatile than Council Tax, with minor reforms in year common. In year losses and gains can be handled through the Collection Fund, with variances from plan can be dealt with by planning ahead for future years	Low/Low  Contingency provided through adjustment of plans for subsequent years.
Other income streams unstable	Actual under-performance in 2014/15 against income targets in sports and leisure centres has been reflected in the proposed budget. Estimates of Income from NHS partners are also downgraded. There is a certain and agreed distribution of the Better Care Fund. On the upside, past performance suggests that unplanned income may materialise, offsetting generally the risks against the aggregate net revenue budget. Unbudgeted income ranged between £1m-£2m in the last two years, but the sources are	Medium/Low  Contingency provided through in-year budget control.  Continuous dialogue with NHS partners over funding flows.

Risk Event	Description and Mitigation in Place	Residual Risk Rating (Likelihood/Impact) and Contingency
		Likelihood: Low <30% <Medium < 70%< High Impact: Low <£2m< Medium < 5m < High
	insufficiently certain to include in the estimates.	
Member support for the budget diminishes	The Executive and individual Portfolio Holders, have been involved at a very detailed level in the development of the proposals agreed in February 2014 and in the development of the amended new and accelerated proposals. The budget is set for 2015/16 only, and while the full year consequences of decisions have been included in the financial estimates, the result of the May 2015 Election will determine future year budgets.	Low/Medium  Contingency provided through adjustment of plans for subsequent years
Plans for implementation of changes are not robust	Each savings proposal is required to be accompanied by a project plan setting out the implementation path. The impact of the plans has been tested in consultation. The degree of risk in each individual proposed change varies, and requires continuous project management.	Low/Low  Contingency provided through continuous improvement of plans, through base budget risk action contingency
Planning is insufficiently flexible to respond to unexpected events	Governance arrangements allow Directors, under delegated authorities, and in consultation with Portfolio Holders, to flex plans during the year. If necessary, recourse can be had to the Executive to approve changes within the overall agreed budget envelope	Low/Low
Implementation of change is poorly controlled, or compromised by insufficient internal capacity	<p>From 2011/12 to 2014/15, the Council has managed to implement savings of £135m. Looking at performance in 2014/15, 93% of specific savings plans are forecast to convert into actual savings (compared with 75% in 2013/14). Given the cumulative impact of the savings since 2010, it will be increasingly hard to find mitigating savings.</p> <p>To improve the conversion rate of specific savings, the standard programme and project management method, which has been adopted across Departments, will continue.</p> <p>The degree of risk varies across Departments. The programme of change for Adult Services continues to be the most risk-laden in</p>	High/High  Compensating action to reduce net costs  Risk action contingency in base, representing 6% of the total specific changes in each year.

Risk Event	Description and Mitigation in Place	Residual Risk Rating (Likelihood/Impact) and Contingency
		Likelihood: Low <30% <Medium < 70%< High Impact: Low <£2m< Medium < 5m < High
	view of: the interconnectedness of the changes; the number and range of stakeholders to be consulted and managed; the statutory framework; the close links between local decisions and nationally-sponsored policy and thinking on new models of health and social care; and recent actual experience of managing change. The package of proposals to reform entitlements to and methods of transporting individuals to and from services has residual risks because the scale of change and the characteristics of the people affected make implementation complex and potentially prone to delay. These risks will be monitored through project management.	
Uncertainties over the integration of health and social care, including delays in developing new models of care to support changes to service delivery	The future of adult social care is heavily influenced by national policy on integration. Work to develop “new models of care” could run slower than is necessary to inform/support local changes, with potential adverse financial and client impacts. To counteract this, existing Governance mechanisms including Health and Wellbeing Board and supporting bodies are in place, allowing shared planning with NHS partners, and joint participation in nationally led initiatives.	High/High  Use of balance sheet to offset financial uncertainty  The Council may have to make unilateral changes if the pace of change is too slow
Changes related to staff cannot be implemented to plan	Consultation with Trade Unions has been extensive, and implementation will focus on avoiding compulsory redundancy. The voluntary redundancy framework has proved to be effective. The total number of staff that could be at risk from this proposed budget is 559, about which the Council commenced consultation with the Trade Unions on 28 October 2013. Staff related changes account for £10.9m (31%) of total budget changes in 2015/16	Low/Medium  Compensating action to reduce net costs  Contingency provided in base budget
Changes related to external suppliers cannot be	The budget proposals foresee a reduction to spending with external suppliers of £15.9m (46%) of total budget changes in 2015/16. Past experience suggests that through individual contract negotiation	Low/Medium  Compensating action to reduce net costs

Risk Event	Description and Mitigation in Place	Residual Risk Rating (Likelihood/Impact) and Contingency
		Likelihood: Low <30% <Medium < 70%< High Impact: Low <£2m< Medium < 5m < High
implemented to plan	budgets can be managed through a combination of volume and price. However, Adult Services have found their supply chain less amenable, and there is active discussion about contract rates for care services.	Contingency provided in base budget
Changes related to income generation cannot be implemented to plan	General economic conditions, and changes in the distribution of the DSG, have contributed to pressure on income budgets in recent years. The proposed budget has rebased selected income lines, and does not require inflationary price rises on income budgets. However, it still assumes total real increases in income of £2.4m (7%) of total budget changes in 2015/16	Medium/Low Compensating action to reduce net costs Contingency provided in base budget
Customer/ citizen behaviour inconsistent with plan	Some changes require higher degrees of change in behaviour from service users; and continuing consultation processes may pose risks to implementation. The consultation to date suggests the most sensitive areas are in Adult Services; and the transport-related proposals. In 2014/15 plans to reduce waste management costs were thwarted by unexpected increases in the volume of waste produced in the District.	Medium/Medium Compensating action to reduce net costs Contingency provided in base budget
Demographic changes place unplanned burden on resources	The proposed budget has been increased to account for £4.3m of demographic growth in Adult Services. The Schools budgets (funded by the DSG) reflect the latest pupil census. As a fast-growing city, it is expected that demographic growth will continue to lead to service pressures, which will need to be factored into future plans.	Low/Low Contingency provided through adjustment of plans for subsequent years
Insufficient inflation allowance	Office for National Statistics data shows the Consumer Price Index inflation running at 0.5% and the Services Producer Price Index at 1.5% (annual figure, as at December 2014). Expenditure budgets have been selectively inflated at indices appropriate for the relevant commodities, ranging from 1% to 1.5%. Where appropriate, budget managers will need to absorb unfunded inflation through reducing consumption of goods and services. Pay budgets have been	Low/Low Compensating action to reduce net costs

Risk Event	Description and Mitigation in Place	Residual Risk Rating (Likelihood/Impact) and Contingency
		Likelihood: Low <30% <Medium < 70%< High Impact: Low <£2m< Medium < 5m < High
	inflated to reflect nationally agreed pay awards.	
Capital investment is poorly controlled	An adequate level of contingency is included in the plan. However, some individual major projects have yet to reach full business case stage, so their cost will need to be monitored. Recent experience suggests that capital projects take longer to implement than implied by the financial plan; but the revenue budget implications tend to be favourable. The sports facilities investment programme requires disciplined management and control.	Low/Low  Contingency provided through adjustment of plans for subsequent years
Sources of funds for capital investment do not materialise	The capital investment plan is partly funded from capital receipts. If they do not materialise, the plan (or individual projects within in which are dependent on receipts) will need to be reviewed.	Low/Low  Contingency provided through adjustment of plans for subsequent years
Internal governance arrangements are not fit for purpose	Constitutional arrangements, internal delegations, and the financial control environment are in place and, from audit testing, are effective. The School Forum and the supporting mechanisms are likewise effective at enabling a mature discussion about the use of local authority and DSG funds to support schools and pupils. Changes in senior personnel mean the loss of continuity of knowledge, but bring the advantage of new perspectives.	Low/low
Governance arrangements with external parties are not fit for purpose	Combined Authority governance to oversee significant capital investment schemes (particularly transport) will change the way in which spending decisions are made, though this is unlikely to increase financial risk. The New Deal programme will likely give rise to new (forms of) partnerships, and they will need to be effective if they are to yield financial viable ideas for 2016/17 and beyond.	Low/Low