

Finance and Resources Committee

10.00am, Thursday 15 January 2015

Council's Budget 2015/16 – Risks and Reserves

Item number	7.8
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. In addition, it provides an update on projected reserves including the Capital Fund for the period 2015/16.

Links

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

Council's Budget 2015/16 – Risks and Reserves

Recommendations

- 1.1 Members of the Finance and Resources Committee are asked to:
 - 1.1.1 note the contents of this report;
 - 1.1.2 remit this report to Council for decision on 12 February 2015 as part of the budget setting process; and
 - 1.1.3 authorise for ratification by Council the allocation of £7.5m from the Capital Fund to support additional capital investment priorities.

Background

- 2.1 Risks are inherent in any budget process. This report advises members of significant risks identified in the budget process, quantifying these where possible, and sets out the range of measures and provisions put in place to mitigate them.
- 2.2 Reserves are held against the risk of unanticipated expenditure or reduced income arising in any particular year. In addition, under accounting rules, some reserves are set aside to manage timing differences between the receipt of income and expenditure being incurred.
- 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.
- 2.4 Whilst the revenue budget framework covers the period 2015 to 2018 and the capital framework 2015/16 to 2019/20, the emphasis within this report is on 2015/16.

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, that the combined effect of the

complexity of the Council's activities and the environment within which it operates means that this list should not be seen as exhaustive.

- 3.2 Risks have been categorised 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

Transformational, organisational reviews, efficiency, income-generating options and procurement

- 3.3 The budget process makes assumptions on the delivery of major projects and the level of savings that can be achieved, including those from internal improvement plans. There are a number of risks that fall within this area:
- the ability to deliver savings already approved by Council that impact in 2015/16, and savings proposals set out in the revenue budget framework for decision on 12 February 2015, within the timescales stated; and
 - the ability to deliver services within the baseline level of available resources.
- 3.4 The budget proposals as set out at the meeting of the Finance and Resources Committee on 30 September 2014, if all accepted and subject to management of other risks and pressures, are sufficient to address the Council's net savings requirement in 2015/16. The final list of agreed options will not be known until February 2015, however, and therefore the risks may vary, depending on the final approved budget.
- 3.5 Given the level of savings targeted through transformational change, procurement and BOLD-themed plans in 2015/16 and future years, regular updates on these critical areas will be provided to the Finance and Resources Committee as part of its work programme. These updates, forming part of wider progress reports on the Council's operational governance arrangements, are geared towards providing due assurance on the robustness of the relevant plans and closely tracking the associated savings. This assessment will also need to consider the level of investment and voluntary release-related costs underpinning the relevant workstreams.
- 3.6 The ICT Transformation programme has up to £7.5m provided through set-aside balances for additional investment to support the transition to a new provider. There are risks around the adequacy of this sum and the current level of provision for any other upfront expenditure associated with the changes such as procurement, development and training costs.

On-going risks

Financial Settlements and wider fiscal policy changes

- 3.7 Whilst details of the financial settlement are known for the 2015/16 financial year, this is a one-year settlement agreement. There is a risk that the actual level of income in future years is lower than the level assumed in the long-term financial plan. The level of funding could vary for a number of reasons, including updated population data, as the distribution formula is complex and covers a wide range of factors. The outcomes from the Smith Commission could also have significant impacts on the future funding arrangements for national and local government. Longer-term assumptions on grant funding are based on best-available estimates of wider public expenditure but are also subject to changes in both Scottish Government priorities and wider UK Government fiscal policy.
- 3.8 Besides grant funding settlements, the budget framework reflects the impact of such factors as the removal of the existing employer's National Insurance rebate in April 2016. There is a risk that further similar changes are introduced as part of addressing the UK-wide structural deficit, placing additional cost pressures on the Council.

Holiday Pay claims

- 3.9 The European Court of Justice ruling in May 2014 requiring overtime and other pay elements to be included in the calculation of holiday pay has resulted in an increase in employee costs in 2014/15. Additional resource of £1.1m was approved by the Finance and Resources Committee on 30 October 2014 and holiday pay arrangements comply with relevant guidance. There is a risk, however, that claims will be made for further backdated payments.

Loss of income

- 3.10 Assumptions on the level of income that will be generated for services are made in the budget process. The risks relate to (i) a decrease in the demand for services for which the Council charges a fee and (ii) the ability to collect all income due.
- 3.11 Whilst these risks cannot be wholly quantified, there are measures the Council can take to mitigate the risk. Such measures include using service level agreements (or similar) for the provision of services to external users and application of the Council's corporate debt policy. Income levels are also subject to regular monitoring and where appropriate the identification of mitigating actions to manage any shortfall.

Demographic changes leading to rising service demands across a range of services

- 3.12 The risk relates to increased demand for such services and the ability to provide for this within the level of available resources.
- 3.13 The budget framework identifies £9.6m in 2015/16 for additional expenditure due to demographic pressures.

Council Tax collection targets are not met

- 3.14 The risk relates to the ability to collect all income due and potential increases in the number of homes entitled to discounts and exemptions. Members are reminded that there can be significant movements in the number of properties entitled to exemptions and discounts, particularly in the latter months of the financial year due partly to the large student population. The revenue budget framework includes the assumption that there will be a further increase in the collection rate of 0.2% in 2015/16. It should be noted, however, that the highest ever in-year collection rate was achieved in 2013/14.

Council Tax Freeze

- 3.15 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.

Infrastructure

- 3.16 The risk relates to there not being sufficient resources to adequately maintain the Council's existing and planned infrastructure, resulting in reduced service provision and / or increased costs in the future.
- 3.17 A further risk relates to the realisation of capital receipts in line with amounts recognised in the capital programme and the ability to deliver and afford the full programme if these do not materialise. The revenue budget framework for 2015-2018 includes £4m of savings from more efficient use of Council buildings and land, a number of which are predicated on disposal of assets.
- 3.18 CMT approved an urgent programme of condition surveys and subsequent safety works in light of the tragic incident at Liberton High School. The extent of this programme and the subsequent potential funding requirement is still to be fully quantified.
- 3.19 The overview of the Local Development Plan reported to this Committee on 7 May 2014 noted the assumption that capital costs would be fully funded by developers' Section 75 contributions. There remains a risk both on the timing and achievement of these contributions which could create a short-term or overall funding pressure.

Large-scale emergencies

- 3.20 The risk relates to the Council requiring to meet the first £1.901m (2014/15 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

- 3.21 Provision of £12.6m has been made within the financial statements to 31 March 2014 for impairment of the debtors balance relating to statutory notices. The Council has also earmarked a further £3.9m in its reserves to cover the costs of any potential further liability claims in respect of statutory repairs. This is reflected in the projected movement in reserves shown in Appendix 2. The current position on billing and recovery is detailed in a report elsewhere on the agenda.

Major Projects

- 3.22 The risk relates to the requirement to meet additional loan charges if the costs of major capital projects exceed approved budget levels. The Corporate Programmes Office assists the Council in mitigating this risk and ensuring best practice is shared across projects.

Universal Credit / Welfare Reform

- 3.23 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. Regular update reports on Welfare Reform are considered by the Finance and Resources and Corporate Policy and Strategy Committees. The impact on the Housing Revenue Account (HRA) will be reported separately as part of the HRA budget process.
- 3.24 There is a risk that demand-led services may exceed available funding and that further welfare changes may have an impact on demand for other council services. The Scottish Government has indicated, however, that it will engage with Local Authorities if it can be demonstrated that expenditure exceeds funding in relation to Discretionary Housing Payments.

Dilapidations

- 3.25 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

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

Tram operations

- 3.27 There is a risk of passenger fares revenue falling below business case assumptions. Projections are subject to ongoing review and will be reported on in detail early in the new year.

Inflation

- 3.28 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.

Emerging Risks

Pentland Hill Care Home

- 3.29 The proposed joint interim care facility – Gylemuir House (formerly Pentland Hill Care Home) will involve a new lease arrangement on the property and associated costs. There is a risk that if combined Council and NHS Lothian funding of £2.8m cannot be secured for 2015/16, the facility will not be able to provide the additional care beds but will still incur the lease costs as detailed in the report to this Committee on 27 November 2014.

Health and Social Care Integration

- 3.30 The functions in scope for Health and Social Care Integration will be delegated to the Integration Joint Board which will be responsible for the governance, planning, operational oversight and resourcing of adult social health and care services in Edinburgh. The Integration Joint Board will need 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 most recent update was reported to Committee on 27 November 2014. There is a risk that funding will be insufficient to deliver the planned outcomes.

Zero Waste Project

- 3.31 Council approved the commencement of the procurement process for the residual waste treatment contract at its meeting on 14 October 2010. Members were alerted to the potential exposure of the Council to legacy contract costs with the incumbent provider during the period 2017/18 – 2019/20.

Reserves

- 4.1 Members are aware that the Council holds a number of earmarked balances within the General Fund. At 31 March 2014, the General Fund balance stood at £123.309m, of which £110.284m was earmarked for specific purposes. The unallocated General Fund balance stood at £13.025m, in line with the medium term strategy. There are planned movements in reserves during 2014/15, with a projected balance at 31 March 2015 of £105.450m.
- 4.2 The current budget does not provide for any further contributions to the unallocated General Fund. The level of this reserve at 31 March 2014, together with the forward strategy, is considered appropriate, in view of the financial liabilities and risks likely to face the Council in the short to medium term.
- 4.3 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.
- 4.4 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.
- 4.5 There are a wide range of commitments on, and potential risks to, the existing level of reserves in the coming and subsequent years. In the absence at this stage of firm longer-term plans, reliance on reserves solely to facilitate additional investment and /or reduce the level of required savings would therefore be considered neither prudent nor sustainable.
- 4.6 The creation of the Strategic Acquisition Fund was approved by Council on 7 February 2013. Funding of £7.5m was to be earmarked from the sale of capital assets not currently supporting the capital investment or property rationalisation programmes. During 2014/15, part-funding of this initiative has been provided by means of a one-off dividend receipt of £3m derived through an asset sale from Shawfair Land Ltd.
- 4.7 Members are reminded of the approval to draw down £5.23m of funding from the reserves, including from the Repair and Renewals reserve, to the General Fund in 2014/15 and 2015/16 to meet pressures within imProvelt and iPFM, as reported to the Finance and Budget Committee on 19 September 2013. It should be noted that there are no planned reimbursements of these sums in 2015-16 but a requirement to refund in the longer term is noted.
- 4.8 The Capital Fund reserve has been built up over recent years to provide flexibility in future years with regard both to savings arising from procurement and as a source of funding for key transformational projects such as the BOLD initiative. The balance at 31 March 2014 stood at £25.835m.
- 4.9 Following a review of the fund, it is recommended that, subject to Council decision, £7.5m be made available from the Capital Fund to support the capital

investment priorities outlined in the report elsewhere on this agenda. Subject to the Committee's approval, allocation of these sums will then form part of the budget proposals presented to members on 12 February 2015.

Measures of success

5.1 Relevant measures include:

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

Financial impact

6.1 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 crystallising.

Risk, policy, compliance and governance impact

7.1 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

8.1 Equality impact assessments are being carried out, where required, on the proposals set out in the Draft Council Revenue Budget Framework 2015-2018. A separate report will be submitted to the February Committee to ensure that members pay due regard to relevant issues in setting the 2015/16 budget on 12 February 2015.

Sustainability impact

9.1 The proposals comprising the budget framework have also been subject to an assessment of their likely corresponding carbon impacts. The results of these assessments will therefore be reported to the Finance and Resources Committee in February to ensure that members pay due regard to them in setting the Council's 2015/16 budget on 12 February 2015.

Consultation and engagement

10.1 A budget consultation and engagement exercise has been undertaken. A separate report will be submitted to the February Committee.

Background reading/external references

[Revenue and capital budget framework](#), Finance and Budget Committee, 19 September 2013

[2015-18 revenue and capital budget framework](#), Finance and Resources Committee, 30 September 2014

[Revenue budget 2015-18 and capital budget 2015-2020 - update](#), Finance and Resources Committee, 27 November 2014

Alastair D Maclean

Director of Corporate Governance

Contact: Hugh Dunn, Head of Finance

E-mail: hugh.dunn@edinburgh.gov.uk | Tel: 0131 469 3150

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 – Risks Matrix Appendix 2 – Planned Use of Reserves Appendix 3 – Purpose of earmarked balances

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, efficiency, income-generation options and procurement	Workforce Reductions – Earmarked provision Procurement strategy / Mitigating action 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
Holiday Pay settlements	Earmarked provision
Demographic changes leading to rising service demands	Long-Term Financial Plan
Council Tax collection targets are not met	Unallocated reserve
Infrastructure	Asset Management Plan / Mitigating Action
Large scale emergencies	Unallocated reserve
Property conservation	Earmarked provision / Unallocated reserve
Major projects	Mitigating action (Corporate Programmes Office) / Long-Term Financial Plan
Universal Credit/Welfare Reform	Long-Term Financial Plan
Dilapidations	Long-Term Financial Plan
Legal Claims	Unallocated reserve
Service area -specific risks	Mitigating action
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

Procurement Strategy – establishment of an approved procurement pipeline

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 31.3.15 £000	Projected Investment / (Withdrawal) £000	Projected Balance at 31.3.16 £000
<u>Unallocated General Fund</u>	13,025	-	13,025
<u>Balances Set Aside to Manage Financial Risks</u>			
Balances Set Aside For Specific Investment	4,351	(2,724)	1,627
Council Priorities Fund	6,607	(3,600)	3,007
Contingency Funding/Workforce Management	22,332	(3,900)	18,432
Dilapidations Fund	8,376	(1,000)	7,376
Insurance Fund	11,470	40	11,510
Strategic Acquisition Fund	3,000	(3,000)	0
<u>Balances Set Aside from Income Received in Advance</u>			
Licensing Income	1,824	4	1,828
Lothian Buses	3,000	(1,000)	2,000
Other Minor Funds	193	(71)	122
Pre-paid PPP Monies	1,580	125	1,705
Recycling Monies	1,374	(500)	874
National Performance Centre	1,996	(1,996)	0
Council Tax Discount Fund	14,257	(4,192)	10,065
Unspent Grants	3,173	(34)	3,139
<u>Balances Set Aside for Investment in Specific Projects which will Generate Future Savings</u>			
IT Transformation	3,777	3,880	7,657
Energy Efficiency	1,015	4	1,019
Spend to Save	3,000	(60)	2,940
<u>Balances Set Aside under Devolved School Management Scheme</u>			
Devolved School Management	1,100	-	1,100
Total General Reserve	105,450	(18,024)	87,426
Capital Fund	25,835	(7,500)	18,335

Balances set aside to manage financial risk	Source/purpose
Balances set aside for specific investment	Funding set aside for specific projects; including improved 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 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.
Recycling monies	Holds monies received by Council through Zero Waste funding.

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	<p>Monies set aside from efficiencies in the ICT contracts for the following purposes:</p> <ul style="list-style-type: none"> (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.
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.

Capital Fund	A usable reserve which comprises receipts from the sale of property. The fund is used for capital expenditure such as purchase of property or repayment of loans.
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