

FINANCIAL RESILIENCE 2016/17

REPORT OF THE CORPORATE DIRECTOR RESOURCES

AGENDA ITEM: 5.2

PORTFOLIO: CORPORATE AFFAIRS

Annexe B of Appendix 6 of this report is not for publication as it contains exempt information of the description in paragraphs 14 and 21 of Schedule 12A of the Local Government Act 1972.

Reason for this Report

1. Financial resilience can be defined as the ability of the Council to meet unexpected or known demands on resources, in the short, medium and long-term.
2. This report provides Audit Committee Members with various items of information that helps support financial resilience and also to provide information and benchmarking data on the Council's Financial Resilience. This includes the items below:
 - Financial Resilience Snapshot - Month 6 2016/17
 - Financial ratios derived from Statement of Accounts on an All Wales basis for 2013/14 and 2014/15 as calculated and published by Welsh Government
 - An Earmarked Reserves protocol for the Council which includes earmarked reserves balances at 31 March 2016.
 - The approach and policy on Minimum Revenue Position as determined by the S151 Officer in terms of the amount to be set aside from revenue budgets as a provision for repayment of debt.

Issues

Financial Resilience Snapshot – Month 6

3. The financial pressures facing local authorities since 2010 have been well documented. The reductions in funding have created financial risks and uncertainty for local authorities, against the increasing financial pressures being experienced by Councils. Whilst a robust financial governance framework exists in local government, the recent economic situation has meant local authorities having to look at financial governance in new ways.

4. Within Cardiff there has been an emphasis on raising the profile of financial resilience including briefings and training sessions for both Members and Officers. The Council regularly prepares Financial Resilience Snapshots which are designed to give an overview of the financial health of the Council at intervals throughout the year. A snapshot is currently produced as part of the :-
 - Budget Proposals report in February each year and
 - Budget Strategy report in July each year
5. The above reports are considered by Cabinet and Council and the intention is also to provide a recurring mid year update to Audit Committee of the snapshot.
6. The snapshot aims to provide an overall view of performance and enable emerging issues and trends to be identified by using past, present and future information and the Month 6 snapshot is included at **Appendix 1**.
7. The information in the Financial Resilience Snapshot is broken down into three parts:
 - The left hand column focusses on historic information taken from the Council's Statement of Accounts 2015/16 and prior years.
 - The middle column provides forecast information for the current financial year at a point in time and in the case of this snapshot this is based on information included in the Budget Monitoring Report for Month 6.
 - The right-hand column includes tables, charts and figures taking a forward look and projections of the financial situation in future years.

Left-Hand Column: Historic Information taken from the Council's Statement of Accounts

Council Fund and Earmarked Reserves

8. This chart shows the amount of Earmarked Reserves and the Council Fund balance held at the end of the financial years from 2012/13 to 2015/16; in quantum as well as a percentage of the Council's net budget. In 2015/16, Earmarked Reserves increased to £51.637 million and the Council Fund Balance increased to £15.255 million. This has been previously reported in the Statement of Accounts and Outturn Report for the year. The year end outturn position provided the opportunity to increase the level of reserves for use in connection with future commitments, in turn improving the Council's financial resilience position.

Historic Cumulative Budget Savings

9. This chart shows both the individuals savings required from 2011/12 to 2016/17 and the cumulative effect of these savings. This shows a total of £163.896 million of savings has been required to be made by the Council over the last six years. This has seen a rise in recent years as a result increasing austerity coupled with increasing demands on services.

Actual Revenue Funding Split

10. This chart provides a breakdown of the sources of funding for the Revenue Outturn position for that year between the Revenue Support Grant, Council Tax, Non-Domestic Rates and other income. The Revenue Support Grant decreased by £3.440 million to £322.851 million between 2014/15 and 2015/16. Non Domestic Rate (NDR) income also decreased by £8.442 million in 2015/16 to £101.253 million. The chart shows the continuing dependency on Central Government funding, changes to which can only be met from savings or increasing Council Tax.
11. Council Tax increased by £6.010 million between 2014/15 and 2015/16 with an outturn of £144.062 million. Council Tax as a percentage of revenue funding is just over 25%.

Financial Ratios

12. Whilst ratios determined from local authority accounts can be used to support benchmarking, scrutiny and challenge of authority finances, there are significant risks to comparison. They should not be used as measures of good or bad performance. Balance sheet data is at a point in time and there are drawbacks to the ratios themselves. There are also accounting and other balances within a Council's accounts which can skew comparisons significantly. Accordingly, comparison should be undertaken with care.
13. The ratios provided in the Month 6 snapshot for Cardiff are based on its single entity Statement of Accounts and are those that have been published by Welsh Government. **Appendix 2** gives a definition of each of the ratios along with a view on any drawbacks of each measure.

Working Capital as % of Gross Revenue Expenditure

14. At 31 March 2016, Cardiff had a Working Capital of 6.02% which is an increase of 0.89% from the previous year. The reason for this is that the current assets have increased slightly by £1.570 million and at the same time current liabilities have decreased by £5.359 million. This is as a result of a number of variables, but the inference is that the Council should be in a better position to cover day to day expenditure.

Usable Reserves as % of Gross Revenue Expenditure

15. At 31 March 2016, Cardiff had Usable Reserves of 10.31% which was a 3.15% increase on the previous year. This reflects the increase in reserves indicated earlier.

Earmarked Reserves as % of Gross Revenue Expenditure

16. Cardiff's ratio at 31 March 2016 was 6.63% which was an increase of 2.35% on the previous year and this follows the increasing trend over the past two years.

Unallocated / General Reserves

17. Cardiff's ratio was 7 days coverage of expenditure which was an increase of 1 day from the previous year and again follows an increasing trend over the past couple of years.

Long-term Borrowing to Long-term Assets

18. The ratio for Cardiff at 31 March 2016 was 0.35 which was a significant increase on 2014/15 considering the previous years had all been relatively consistent between 0.22 and 0.25. This reflects the £187 million Housing Subsidy Settlement Payment to Welsh Government funded by borrowing.

Long-term Borrowing to Taxation and Non-Specific Grant Income

19. The long-term borrowing to taxation and non-specific grants ratio for Cardiff for at 31 March 2016 was 1.05 and again this was an increase on the previous year as which was 0.72. This is as a result of the Housing Subsidy Settlement Payment.

Council Tax as % of Taxation and Non-Specific Grant Income

20. At 31 March 2016, Cardiff had a ratio of 27.68% which was an increase of 2.04% from the previous year's ratio of 25.64%.

Middle Column: Forecast information for the current financial year

Revenue Month 6 Projected Position

21. The Month 6 Budget Monitoring report was considered by Cabinet on 21 November 2016 and the forecasts included in the snapshot are consistent with that report. In total the Directorates collectively have a projected outturn over budget on revenue expenditure by 1.26%.

Revenue Savings Achieved and Unachieved as at Month 6

22. This shows the total level of savings for 2015/16 which were £32.473 million. Out of this 88.5% were achieved, 6.1% were written out as no longer technically achievable, and 5.4% were unachieved at that stage. In 2016/17, the total £28.835 million to be achieved shows that 80.5% of the savings are projected to be achieved and 19.5% are currently projected to be unachieved.
23. The unachieved savings for both years has been broken down by Directorate. For 2015/16, this shows that Social Services has the highest level of unachieved savings. The projection for 2016/17, shows Social Services, City Operations and Economic Development all with unachievable savings of over £1 million for each Directorate. Monitoring of savings is ongoing in the current year with regular consideration at Senior Management Team and timetabled discussion with Cabinet Members.

Capital Month 6 Projected Position

24. This table reflects projections in the Month 6 Budget Monitoring report. The largest variance relates to Education & Lifelong Learning and primarily to timing of costs expected in relation to the new Eastern High School and three new primary schools.

Right-Hand Column: Financial Snapshot of Future Performance and Estimates

Medium Term Financial Plan

25. This table outlines the budget reduction requirement that the Council is facing over the medium term, along with a summary of the strategy proposed to address this. The budget reduction requirement is the sum of the financial pressures facing the Council and the projected funding reduction for each year. In order to address the gap, budget strategy assumptions are added to total projected savings. Any remaining gap which is still to be addressed is shown in the final row of the table.

Capital Expenditure & Capital Financing Requirement

26. This table sets out the estimates for capital expenditure and historic capital expenditure incurred but not yet paid for (the Capital Financing Requirement) for the next three years. Figures for 2017/18 onwards are those included in the Budget report for 2016/17.

Affordability Indicator – Capital Financing Costs as a % of Controllable Budget

27. Capital financing costs include external interest payable and prudent revenue provision. The affordability indicators were established in 2011/12 and the percentages for that year are used as a base for determining the increase in this ratio over a period. Future years' projections are those currently included in the Budget report for 2016/17.

Financial Ratios – WG Comparative Data

28. Welsh Government have recently started to publish reports on Local Authority Financial Indicators. The financial indicators for 2013/14 and 2014/15 for all Local Authorities in Wales are shown in **Appendix 3** along with any interpretation of those ratios by the Council. Data using 2015/16 accounts yet to be published by WG.
29. It should be noted that the All Wales ratios are based on the audited Whole of Government Accounts submissions whereas the information included in the Council's snapshot is based on the Council's single entity accounts. The risks and limitations of comparison and any interpretation in the **Appendix 3** should be noted.

Earmarked Reserves

30. Reserves are amounts set aside for specific policy purposes or for general contingencies and cash flow management. There may be earmarked or general reserves.
31. Reserves enable Councils to:
- Create a working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this forms part of general reserves;
 - Create a contingency to cushion the impact of unexpected events or emergencies. This also forms part of general reserves.
 - Creates a means of building up funds, often referred to as earmarked reserves, as defined above, to meet known or predicted liabilities.

32. CIPFA recommended accounting practice requires the S151 officer to create a protocol for reserves and balances for each reserve established. This should set out the purpose, usage and the approval processes for transfers in and out of reserves. This needs to be clearly defined, along with the processes for determining whether the intended use of the reserve is still valid. The current protocol used by the Council is included in **Appendix 4**. **Appendix 5** shows the position for all earmarked reserves at 31 March 2016, this information has come from the Statement of Accounts 2015/16.
33. The annual Budget Report to Council includes an assessment by the Section 151 Officer of the adequacy of reserves. The statement included in the 2016/17 report was that “the judgement of the Council’s Section 151 Officer, taking into account the budget monitoring forecast as at 31 December 2015, the corporate budget position, the General Reserve, as well as the General Contingency budget of £4 million, is that the projected level of both general and earmarked reserves up until 31 March 2017, is adequate when considering the 2016/17 budget”.

Minimum Revenue Provision (MRP)

34. The Council has a Statutory Duty to set aside each year from its annual revenue budget an amount ‘which it considers to be prudent’ towards the eventual repayment of the Capital Financing Requirement (CFR) / Borrowing (Local Authorities (Capital Finance and Accounting) (Wales) Regulations 2003. This is known as the Minimum Revenue Provision (MRP) and it is the method of spreading the cost of capital expenditure funded by borrowing.
35. Similar to decisions to undertake capital expenditure funded by borrowing, decisions in respect of the allocation of MRP have short, medium and very long term impacts. Impacts of changes in policy decisions should be considered over that time horizon and need to consider the impact on current and future generations. The introduction of the Well-being of Future Generations (Wales) Act 2015 serves only to underline the importance of decisions such as the MRP and these will be scrutinised by Wales Audit Office.
36. As such those decisions are not easy ones, but need to consider a range of factors, professional advice and judgement.
37. This report focuses only on one aspect of the MRP, and that is the Council’s approach to MRP on Supported Borrowing, i.e capital expenditure which is supported by WG in the annual Revenue Support Grant received from WG.
38. **Appendix 6** and its Annexes provides a range of information to support the Council’s approach to MRP on supported borrowing. It includes:-
 - Key definitions to aid understanding
 - Outlining the Regulatory requirements in respect of MRP
 - The Council’s previous reviews and approaches to MRP
 - Different approaches recently being undertaken by local authorities that result in short term savings
 - Factors considered in developing a recommendation and
 - Recent regulatory comments on different approaches

39. In the 2016/17 Budget Report, it was determined having considered the advice of the S151 Officer that Council Fund historic expenditure prior to 1 April 2004 as well as subsequent supported borrowing approved by the WG is to be provided at 4.0% on a reducing balance basis in 2017/18, a reduction from the 4.5% figure for 2016/17 and previous years. This is consistent with the support provided by WG as part of the Revenue Support Grant for supported borrowing. For the reasons stated above this approach will continue unless WG changes the approach to providing support as part of the Revenue Support Grant formula or any revision to MRP Guidance either in Wales or in England albeit regular reviews of the position will continue.

Reason for Recommendations

40. To allow Audit Committee to consider a range of performance, benchmarking information and policy information.

Legal Implications

41. No direct legal implications arise from this report.

Financial Implications

42. Financial standing and resilience is an important element of the Council's financial governance arrangements. The Council's 2016/17 budget report included a significant section running to 35 paragraphs concluding with the Section 151 Officer's statement. "Overall the position in respect of risk and reserves will require careful monitoring throughout the financial year, particularly in light of the achievability of savings and further financial interventions may need to be considered. Beyond this, given the information and uncertainty contained in the MTFP, the position with regard to reserves will continue to be carefully monitored alongside the Council's general standing in respect of financial resilience."
43. Cabinet received on the 10 November a report outlining the 2017/18 Budget Proposals for consultation. The report confirmed that the Provisional Settlement from Welsh Government was for one year only with no indicative figures beyond 2017-18. The absence of multi-year settlement figures inhibits the ability to ensure that financial plans address the challenges of the medium and long term. However, current assumptions in the Council's Medium Term Financial Plan set out a budget gap of £76 million with a sensitivity analysis increasing this to £99 million. In considering the financial policies of the Council, the S151 Officer must take into account the risks to the financial standing of the Council in the long term as well as the responsibilities arising from the introduction of the Well-being of Future Generations (Wales) Act 2015. This report has set out the main components to the Council's approach to reviewing, safeguarding and improving financial resilience.

RECOMMENDATIONS

44. That the Audit Committee notes the report and agrees to continue to receiving regular updates on financial resilience

CHRISTINE SALTER
COROPORATE DIRECTOR RESOURCES
17 November 2016

The following appendices are attached:

Appendix 1 – Finance Snapshot - Month 6

Appendix 2 – Financial Ratios – Definitions and Drawbacks

Appendix 3 – Financial indicators for 2013/14 and 2014/15 for all Local Authorities in Wales
(Welsh Government Data)

Appendix 4 – Earmarked Reserves Protocol

Appendix 5 – Earmarked Reserve Balances 2015/16

Appendix 6– Minimum Revenue Provision (MRP) for Debt Repayment – Supported
Borrowing