APPENDIX K

Report of	Meeting	Date
Chief Finance Officer	Special Council	26 February 2019

REPORT OF THE CHIEF FINANCE OFFICER

PURPOSE OF REPORT

1. To provide advice to the Council as required under s25 of the Local Government Act 2003.

RECOMMENDATION(S)

2. The Council are recommended to note the Chief Finance Officer's comments and advice under Section 25 of the Local Government Act 2003 as set out in this report and have regard to it when considering the budget proposals for 2019/20.

EXECUTIVE SUMMARY OF REPORT

3. This report is required by statute and the Chief Finance Officer should report to members the robustness of the budget estimated including how they have been constructed and the assumptions that underpin them. In addition the Chief Finance Officer must report to members the adequacy of the proposed financial reserves.

4. This report outlines the key assumptions and risks contained in the budget and identifies that over time working balances will be increased to mitigate some of those risks.

5. The Final Local Government Finance Settlement 2019 was published on 29 January 2019. Chorley Council has benefitted from becoming a member of the Lancashire Business Rates Pilot as well as not incurring £156k of negative RSG as previously proposed by the Government. In addition, the Government did not increase the deductions from New Homes Bonus allocations that were proposed as part of the provisional settlement.

6. The government has recently announced an end to austerity however it is my view that the Government will have to reduce funding from district councils and transfer some to upper tier authorities, many of which are struggling to fund adult social care and children's services. In addition, further funding is required to meet the increasing demand for NHS services. It is therefore my view that the increased funding made available to the council in 2019/20 may be a one-off and the results of the fair funding review will mean a reduction in funding for the council in 2020/21 onwards.

7. In terms of the 2019/20 budget once again all key budgets have been reworked to align with expected outturn for 2018/19 and therefore reflect the ongoing cost of delivering the current levels of service. The budget contains expenditure savings targets and increased budgeted income. All expenditure savings included in the 2019/20 budget have been achieved or will be achieved before the end of 2019/20.

8. There continues to be income targets contained within the budget; these are based upon contractual agreements or have been realigned to reflect the latest performance information. A fees and charges report was approved by Executive Cabinet on 17 January 2019 that included increases in some of the charges the council makes for its services. A prudent estimate of £100k increased income has been brought into the budget for 2019/20 onwards. Market Walk will continue to be the council's biggest income generator in terms of fees and charges. There has been an increase in voids in 2018/19 and a fall in some rental levels. The shopping centre however continues to generate £900k net income annually for the council but to mitigate some of the risks to income, revenue budgets are being set aside into an equalisation account to be used should rental targets not be achieved. The balance in the income equalisation reserve will be £440k in 2019/20.

9. The forecast is that the budget will be balanced in 2019/20 and that the Council's general fund balances will be £4.0m. Large risks to the revenue budget include the new revenue generating capital projects that are opening in 2019 as well as the local NHS hospitals outstanding challenge for mandatory rate relief. In addition, funds continue to be set aside as earmarked reserves in 2019/20 that will:

    - help enable the council to implement the Transformation Strategy and resultantly the budget strategy included in the MTFS
    - help mitigate some of the risks within the current and proposed new business rates system.

10. Key risks remain, in particular the forecasting of business rate receipts in 2020/21 onwards. The council will benefit from being a member of the Lancashire Business Rate Retention Pilot in 2019/20. However the 2020/21 75% retention scheme may not resemble the 2019/20 pilot scheme. As such the benefit in 2019/20 will be treated as a one-off and only growth that is achieved in the business rates base will be built into the base budget. There is zero percent growth assumed in the short to medium term period.

11. For the first time the council is required to submit a Capital Strategy that demonstrates that the council's capital expenditure and investment decisions are taken in line with corporate objectives and take account of stewardship, value for money, prudence, sustainability and affordability. I am satisfied the report, Appendix H to the main budget report, provides this assurance to members and outlines what the strategic intent is for the council over the medium to long-term.

12. Having reviewed the underlying assumptions and commented on the position in relation to key risks and working balances I am satisfied that the budget assumptions are reasonable, the key financial risks have been considered and the budget is deliverable.

13. Further analysis of the risks to revenue and capital budgets are analysed at the end of this report.

Confidential report Please bold as appropriate	Yes	**No**

CORPORATE PRIORITIES

14. This report relates to the following Strategic Objectives and to the Council's ability to deliver its corporate plan whilst ensuring a balanced budget is achieved. The MTFS sets out how Council resources will be used to deliver those priorities.

Involving residents in improving their local area and equality of access for all	✓	A strong local economy	✓
Clean, safe and healthy communities	✓	An ambitious council that does more to meet the needs of residents and the local area	✓

BACKGROUND

15. Under the requirements of Section 25 of the Local Government Act 2003 the Chief Finance Officer is required to advise members when setting the budget as to the robustness of the estimates and the adequacy of working balances.

THE ROBUSTNESS OF ESTIMATES

16. In terms of the budget proposals, once again in 2019/20 a thorough reassessment of the budgets has been undertaken by budget holders, service managers and directors and their accountants based upon the latest information available. In terms of the key assumptions contained particularly in the 2019/20 budget these are shown in the main budget report but are summarised for convenience below

KEY ASSUMPTIONS

17. The table below shows the key assumptions made in forecasting forward the Council's financial position.

Key Assumptions	2019/20	2020/21	2021/22
Growth in Council Tax Base	1.42%	1.50%	1.50%
Council Tax Increases	2.99%	2.00%	2.00%
Growth in Retained Business Rates	0%	0%	0%
New Homes Bonus Baseline Adjustment	0.4%	0.4%	0.4%
Total Forecast New Homes Bonus	£2.790m	£2.196m	£2.097m
Future Service Pension Rate	14.4%	17.1%	17.1%
Additional Business Rates - Lancashire Pool	(£0.676m)	£0.000m	£0.000m
Additional Business Rates - Lancashire Pilot	(£0.360m)	£0.000m	£0.000m
Income from LCC	(£0.236m)	(£0.096m)	(£0.096m)
Pension Fund Deficit Recovery	£0.966m	£0.781m	£0.831m
Pay Award	2%	2%	2%

In terms of the key assumptions I would make the following comments to confirm their validity:-

COUNCIL TAX INCREASES

18. Taking into consideration the reductions in funding the council is expecting to experience in 2020/21 to 2021/22 the administration is proposing to increase council tax by 2.99% in 2019/20. As well as this the MTFS models the forecast impact of a 2.00% council tax increase in 2020/21 and 2.00% in 2021/22. As the council tax charge is decided annually it will be for the council to determine if any actual increases are implemented. A prudent 1.5% expansion of the council tax base, excluding council tax increases, is being assumed. This growth is lower than has been experienced in most of the previous years and although it is expected that housing expansion will slow, it is still expected that council tax yield will be greater than budgeted.

REDUCTION IN GRANT SETTLEMENT AND BUSINESS RATES RETENTION

19. With the elimination of RSG, the forecasting of business rates income remains the key funding risk to the council in 2020/21 onwards. The council will benefit from being a member of the Lancashire Business Rate Retention Pilot in 2019/20. However the 2020/21 75% business rates scheme may not resemble the pilot scheme. The final

Government scheme may for example provide more of the retained rates to upper tier authorities. The new scheme may also build in New Homes Bonus allocations and the look to remove it over the short term, this is a large risk to the council as NHB allocations stands at approximately £2m per year.

20. The budget report explains the volatile nature of this particular core income stream and why accurate forecasting of future receipts is problematic. The income levels contained within the retained business rates budget are based upon a set of assumptions that may impact on the total amount collected in future years, in particular the outcomes within the appeals process.

21. The council holds a provision to mitigate the impact that appeals have on the business rates collection fund, including the backdated impact on the council's resources. It is possible that any slowdown experienced as a result of Brexit could result in businesses appealing against their rateable value. The current provision has been increased by £1.2m to £2.9m which represents 4.7% of Chorley Councils annual business rates liability and is comparable with other district council provision. Growth in business rates may be offset by losses on appeals and for this reason I am building no estimated growth into any future years forecast which I believe is a prudent approach.

22. A large risk associated with business rates income relates to two applications for mandatory charitable relief received from Lancashire Teaching Hospitals NHS Foundation Trust. If successful the application would be backdated to 2010 and therefore have a significant negative impact on the Council's revenue budget. A headline figure is a potential £2.4m impact on the Council's general fund and an approximate £280k further reduction in ongoing retained business rates. At present, as per advice from Local Government Association legal advisors, I have assumed this request for relief will not be granted. However I am confident the Council has sufficient general fund balances to deal with the risk posed from these applications.

NEW HOMES BONUS

23. The deadweight adjustment has not been changed in 2019/20 but the Government has not ruled it out for 2020/21 onwards. In order to be prudent I have modelled a reduction in NHB based upon a lower growth in housing stock. The larges risk to NHB is that it is built into the 2020/21 business rates baseline calculation and removed from the council's funding streams in the short to medium-term. NHB allocations total nearly £1bn across all councils. As such, it is assumed that a transitional arrangement will be introduced to help council's manage reductions in funding.

BORROWING

24. In December 2018 £6m of PWLB borrowing was taken to ensure the council managed its cash balances whilst mitigating against potential increases in future interest rates The assumption built into the 2019/20 forecast is that the internal cash balances will not be sufficient to manage the cash flow requirements of the council, especially as the council continues to invest in large scale capital projects. It has been assumed that the council will borrow £20m in early 2019/20.

25. So long as the internal cash position remains positive the council will temporarily continue to internally finance some of the debt required rather than borrow. The rationale for this approach is that the interest earned on deposits is significantly less than borrowing costs and in treasury management terms is financially advantageous to the council. However I need to be able to respond to what happens in the financial markets and as borrowing rates fluctuate be able to react. If rates are forecast to change it will be appropriate to take on some additional borrowing. For this reason, although I have built in some savings, I have also left some headroom for in year borrowing.

PENSION FUND CONTRIBUTIONS

26. As part of a triennial pension review the Lancashire County Pension Fund (LCPF) announced an increase in employer pension contributions for 2017/18 to 2019/20 to meet the future costs of the scheme. The contributions have increased from 11.1% to 14.4% resulting in an increase in the council's contribution of approximately £250k per annum. It is assumed that contributions will increase again to 17.1% in 2020/21 as per the provisional advice from the pension fund.

27. The pension deficit recovery period is assumed to be made over 19 years however Chief Finance Officer's in Lancashire have raised queries to the LCPF as the pension fund as a whole is now fully funded. Chorley Council's element of the fund is still in deficit however the contributions should fall. To be prudent I have assumed any increased cost from rises in the contribution rate will be offset by reductions in the contribution to the deficit.

PAY AWARD

28. A final settlement pay settlement has been agreed and built into the 2019/20 budget. Similar pay increased have been assumed in 2020/21 onwards with higher increases for those on lower salaries.

MEDIUM TERM FINANCIAL STRATEGY

29. The MTFS sets out the Council's plans to bridge the funding gap as summarised below:

Chorley Borough Council Transformation Programme

	2019/20 £m	2020/21 £m	2021/22 £m
Adjusted Budget Deficit/(Available Resources)	**(0.575)**	**1.196**	**1.672**
Contract Savings			
Leisure Centre Management (expires October 2020)	-	(0.217)	(0.446)
Income Generation			
Market Walk Extension	(0.125)	(0.300)	(0.300)
Strawberry Fields Digital Hub	-	(0.139)	(0.174)
Primrose Gardens Residential Village	-	(0.006)	(0.014)
Parking Income	-	(0.180)	(0.180)
Employment Sites	-	-	(0.200)
Total Income Generation	**(0.125)**	**(0.625)**	**(0.868)**
Efficiency Savings			
Efficiency Savings	(0.085)	(0.355)	(0.358)
Adjusted Budget Deficit/(Available Resources)	**(0.785)**	**0.000**	**0.000**
Commercialisation of Council Owned Assets	0.485	-	-
Support for Local Businesses & Corporate Priorities	0.300	-	-
Final Budget Deficit/(Available Resources)	**0.000**	**0.000**	**0.000**

30. The strategy shows that broadly speaking the administration will attempt to bridge the gap by generating efficiency savings and additional income of £1.672m. Based upon the analysis of risk I have undertaken this is not unrealistic but it will require the council to ensure the income generation projects are brought forward as quickly as possible ensuring that they generate the required returns.

31. Investing in income generating schemes is forecast to generate the Council £868k of additional income. It is recognised that this will require significant early expenditure and this is why the Council has set aside £700k in an earmarked reserve specifically for investment in income generating projects. New posts have been recruited and external expertise commissioned to drive forward the expansion of income generation, this includes the development of council owned employment sites that were acquired in 2016/17.

32. The level of income modelled within the income generating projects assumes a gradual increase in occupancy rates. The occupancy rates are ambitious but not unrealistic given the interest already received at Primrose Gardens and Strawberry Fields especially. Further analysis of the risks associated with these investments is given in Appendix H to the 2019/20 budget report.

LEVELS OF WORKING BALANCES

33. The 2017/18 MTFS indicated that working balances should be no less than £4.0m by 2018/19. This level was based upon risk contained in the budget particularly around:
    - the volatility in the funding system in relation to business rate retention
    - possible re-profiling of savings and income generation proposals into future years
    - risk of loss of deposits should a future banking crisis occur

34. In relation to the Treasury Strategy, individual deposit levels were increased to £3m to enable better rates to be accessed, but investments of up to £4m can be placed with part-nationalised UK financial institutions. One of the lessons for Councils who were affected by the Icelandic banking crisis was that they should at least have the minimum level of working balances to cover any potential loss of deposits should a banking crisis occur. For this reason I think it appropriate to keep working balances to a minimum of £4m.

35. There are risks to revenue budgets surrounding the major capital projects that will begin to generate income in 2019/20. These include the possibility that occupancy rates for Market Walk Extension, Strawberry Fields or Primrose Gardens are lower than budgeted in the MTFS. In addition to this, there continues to uncertainty surrounding the United Kingdom's withdrawal from the EU. Further analysis is provided in Appendix F to this report. I deem the general balances of £4m is prudent given these risks.

IMPLICATIONS OF REPORT

36. This report has implications in the following areas and the relevant Directors' comments are included:

Finance	✓	Customer Services	
Human Resources		Equality and Diversity	
Legal	✓	Integrated Impact Assessment required?	
No significant implications in this area		Policy and Communications	

COMMENTS OF THE STATUTORY FINANCE OFFICER

37. These are contained within the report.

COMMENTS OF THE MONITORING OFFICER

38. The report is designed to ensure that the relevant legislation is complied with in terms of Statutory Officer advice.

GARY HALL
CHIEF EXECUTIVE

There are no background papers to this report.

Report Author	Ext	Date	Doc ID
Gary Hall	5151	13/02/2019	

RISKS TO MEDIUM TERM FINANCIAL STRATEGY

The Medium Term Financial Strategy outlines how the Council will achieve its corporate strategy priorities whilst recognising the budgetary pressures it will experience over the coming 3 years. Within the strategy are a number of risks that are outlined below.

RISKS TO REVENUE BUDGET

HIGH RISK

75% Business Rates Retention
The government continues its ambition to implement a new 75% business rates retention scheme for all local authorities by 2020/21. The current pilot is expected to benefit the council in terms of retaining more NDR income. However the final scheme will differ predominately for two reasons:

- The current pilot uses historic baseline funding levels; however the result of the government's fair funding review will see this baseline adjusted with the potential for Chorley Council to receive less of its retained NDR income.
- The government may introduce a less favourable split between lower and upper tier authorities (in the current pilot 56%/17.5% lower/upper split) meaning more of Chorley Council's retained business rates income is paid to LCC
- It may be that New Homes Bonus (NHB) is brought into the baseline calculation and removed in the short to medium term. Chorley Council receives £2m per annum in NHB which is relatively large given its total budget. Removing this grant represents a large risk to the council however it is assumed that if the grant were removed the Government would have to introduce some transitional funding arrangements.

The government is consulting about the reforms due to be implemented in 2020/21, and there is a deadline for responses of 21 February 2019.

NHS Request for Mandatory Relief
A large risk associated with business rates income relates to two applications for mandatory charitable relief received from Lancashire Teaching Hospitals NHS Foundation Trust. If successful the application would be back dated to 2010 and therefore have a significant impact on the council's revenue budget. A headline figure is a potential £2.4m impact on the council's general fund and a further c£280k reduction in ongoing retained business rates. The LGA is representing affected councils nationwide and retain the view that NHS trusts and foundation trusts are not charities and therefore not eligible for mandatory non domestic rate reliefs.

MEDIUM RISKS

Business Rates Appeals and Other Business Rates Adjustments
The Council's provision for business rates appeals stood at £1.65m at the beginning of 2018/19. During the year there has been approximately £400k of successful backdated appeals charged to the provision.

In April 2017 a new business rates appeal process has been introduced called 'Check, Challenge and Appeal'. The benefit of the multi-stage process is that it requires businesses to complete its own 'Check' and therefore should discourage speculative appeals. To date there has been no successfully challenged appeal reported by the VoA against the 2017 list. The VoA has focussed on clearing the backlog of prior year appeals and so it is prudent to assume more appeals will be coming through from the 2017 list in 209/20.

The budget for 2019/20 includes a provision of £2.9m. This is deemed sufficient to meet the potential successful appeals that may transpire from the outstanding list.

Pay Inflation
The MTFS includes an estimated 2% pay increase from 2019/20 onwards with significantly higher pay increases for staff on lower spinal points. In addition the effects of the national review of the National Joint Committee (NJC) pay spine have been brought into the budget. Chorley Borough Council is a member of the Living Wage Foundation and therefore pays a higher rate than the required national minimum wage.

The local government trade unions have accepted the 2019/20 pay offer from employers. Chorley Council has modelled for a 2% pay increase year on year over the MTFS period. Every 1% increase in pay increases council expenditure by £120k.

New Major Projects
The assumptions in the revenue budgets relating to the council's major capital projects are outlined in the Capital Strategy report. The income profile for these projects estimates a total of £2.5m income by 2021/22. The revenue models for these projects include a gradual increase in occupancy rates, these assumptions are ambitious but not unachievable given the interest the council currently has in filling these units. However there remains a risk that slower than budgeted occupancy will impact on the revenue budget. This will be managed through the in-year budget and through the general fund.

Universal Credit
The Government is consolidating a number of welfare benefits into a revised Universal Credit Scheme. One of these is housing benefit which is currently administered by the Council. Universal credit will be managed by the Department of Work and Pensions. The full scheme was rolled out in Chorley in July 2018 however take up has been slow. There is the potential risk that bad debts will increase when people move to UC as it becomes more difficult to recover overpayments. This is because the housing benefit element of debt might not have the same priority over other debt recover such as fuel or rent arrears. Currently there has been very little sign up to universal credit however as take-up increases there is a possibility that the council's bad debt provision will need to be increased with a subsequent charge to the general fund.

Delivery of Budgeted Savings and Additional Income
The MTFS includes a number of challenging saving proposals and innovative plans for income generation. Achieving these goals will require a change in organisational culture, enhanced sharing of services across organisations and commercial negotiations. The monitoring and robust challenge of all proposals is overseen by the council's Transformation Board. Risks are reported to senior management team as well as members and actions taken when required. Given the council's increased dependency on generating income there will always be risks that sit outside of the council and are therefore more difficult to manage.

The council's general fund balance of £4m has been set such that potential delays in bringing forward income or generating savings can be temporarily managed within council resources.

LOW RISK

Inflation
The council's expenditure is subject to annual inflation based on indexation that is determined by external stakeholders. Sharp increases in inflation would result in higher day to day expenditure and possible budget overspends. Inflation forecasts from the Office of National Statistics (ONS) have been used to inform the budget over the coming 3 years. This will be reviewed annually to ensure budgets are sufficient to meet inflationary pressures.

Existing Income
The major income streams the council benefits from include car parking, planning as well as commercial income from units the council owns including Market Walk Shopping Centre. Uncontrollable reductions in income could leave services under-funded. The council has been prudent when budgeting for income and there is relative certainty from the income gained through lease of commercial units. There has been £440k set aside to manage any in-year reductions in income from unbudgeted voids at Market Walk and the planning budget has been reduced by £100k to better reflect forecast activity.

Interest Rates
As a result of the capital investment in the borough the council does not hold large cash reserves and therefore changes in the rates on deposits do not represent a large risk to the council. Potential increases in the rate of PWLB borrowing may result in the council taking long-term borrowing earlier to ensure it finances its capital programme at the most economical rate. The Financial Accounts team monitor changes in PWLB rates closely as well as receiving updates from our treasury management specialists. This enables the team to regularly update and advise the Chief Finance Officer.

RISKS TO CAPITAL BUDGET

MEDIUM RISKS

Overspends on Capital Projects
All capital projects are monitored on at least a quarterly basis, with the major capital projects monitored on an ongoing basis by council officers and commissioned external project managers. Any potential overspends are highlighted by the relevant project group or officer and reported to the Chief Finance Officer.

Actions plans are agreed to manage potential overspends and managed by the project officer. If necessary, financing is identified within the capital programme to meet any additional required resources. Changes to the capital programme are reported quarterly to Executive Cabinet. Changes to a capital project between these periods are taken on a separate report to Executive Cabinet or Full Council.

LOW RISK

Insufficient Financing to Delivery Capital Programme
The council continues to have a significant gap between its capital funding requirement and current borrowing levels. As such borrowing is available to the council if funding sources previously allocated to projects no longer become available.

Insolvency of Major Contractor
As part of the tender process the financial standing of each contractor has been thoroughly assessed. These checks are regularly and the council's subscription to a credit check agency provides alerts were the credit status to change.