Report of the Service Director Finance

Agenda Item No:
Meeting: 14 October 2009

NORTH LINCOLNSHIRE COUNCIL

CABINET

OCTOBER BUDGET REVIEW 2009

1. **OBJECT AND KEY POINTS IN THIS REPORT**

1.1 The council monitors spending against budget month by month throughout the year, with a formal report to cabinet at regular intervals. This budget review report provides an opportunity to take stock of the spending position in revenue and capital budgets and to track operational performance.

1.2 The operational measures include National Indicator (NI) 179 which measures the level of efficiency savings achieved against target; and measures of treasury activity covering council borrowing and investment.

1.3 Where necessary the cabinet may approve resource changes within the cash-limited budget to address emerging issues. A number of proposals are made in this report.

2. **BACKGROUND INFORMATION**

2.1 This report is to help cabinet to track expenditure and income for council services in the current financial year 2009/10. It is an opportunity to consider areas of overspending, and identified savings.

2.2 The council set a cash limited budget for its general fund services at its meeting in February 2009. This puts a limit on service revenue spending and provides a separate contingency for areas of spending where the costs are uncertain. This year the contingency provides for: the 2009 local government pay award (£1.533m); the recession (£0.500m); and for energy cost increases (£0.400m). This contingency is available to assist services in meeting some of their cost pressures. However it is expected that services take their own steps to keep within approved budgets and there is no presumption that the contingency will be applied.

2.3 The report also provides a review of progress on the capital investment programme. Typically, capital schemes have a long lead-time and for larger schemes implementation usually takes place over more than one financial year. This means that in practice the council regularly has to review the phasing of scheme spending from one year to the next, when original timescales prove to be too optimistic. Provided that funding is not time-limited, rephasing does not bring a financial penalty. Of more concern are schemes where spending is projected to exceed budget and where remedial action is necessary.

2.4 The third area it covers is the council's efficiency savings target for 2008/11 and the requirement to confirm the target for 2009/10.

2.5 Finally it reviews the management of the council's cash flow against the criteria and targets set in the treasury management strategy. This includes planned borrowing and investment.

3. OPTIONS FOR CONSIDERATION

Revenue

3.1 The revenue position is shown at Appendix 1. It presents a forecast of spending on services compared to the annual budget. It then looks at the different elements of the forecast and identifies how the different spending pressures can be contained.

3.2 The first element is the effect of the recession on general fund. As expected there are further income shortfalls in a number of areas including school meals, leisure facilities, car parking and planning. Some provision was made for lower income in the original service budgets, but the scale of shortfall in 2009/10 is now clearer. The forecast £0.748m can be covered in part by the £0.500m recession contingency, with services to find the balance.

3.3 The second issue is additional spending which can be funded from earmarked reserves with no impact on the general fund. This includes additional in-year spending on the BSF and waste procurement projects. The council created a specific revenue support reserve to cover the procurement and management costs of these projects.There is also an increased call on the property trading account to offset reduced income and increased costs on the commercial property portfolio. Together these total £0.725m.

3.4 An increased use of the reserves this year means there will be less for future years (see appendix 1A). This could have budget implications if future costs exceed the reserves available. The current forecast is that the property trading account surplus built up in previous years will be fully used by the end of 2009/10.

3.5 The third element is fuel cost inflation. A separate contingency of £0.4m was created for energy cost inflation which has seen substantial volatility in the past three years. Many of the council's contracts are renegotiated from October each year and can now be evaluated. An increase in budget £0.166m is required to cover the costs of electricity for street lighting in 2009/10 and therefore a one-year virement from the contingency is appropriate.

3.6 The final element includes other service cost pressures, some of which are short term (one-year) others longer (base issues). Base cost pressures identified in 2009/10 (£0.39m) are not recession related and would require year on year funding if not resolved. These include a shortfall on target efficiency savings from business process reengineering, and additional running costs in leisure and cultural services. These total £0.463m and are for services to address individually. Together with the proportion of recession costs which services will have to find themselves (para 3.2) there is a cost pressure of £0.711m which services will be required to contain.

3.7 One further element of the contingency provides for the 2009/10 local government pay award. This has now been settled at 1%, with increases of up to 1.25% for lower grades. The cost is £0.925m which can be approved for transfer to service budgets. This leaves a balance of £0.608m in contingency to cover other eventualities which may arise later in the year.

3.8 Schools are a separate issue as they manage their own finances under delegated management and hold their own balances. Collectively these stand at £2.246m. Currently secondaries which are in deficit are working to recover their position; primaries which have surpluses in excess of the guideline 8% of budget are working to reduce them. The current forecast is for a net withdrawal of £0.4m in the current year.

Impact of the 2009/10 position on reserves and future prospects

3.9 The impact of spending in 2009/10 on reserves is shown at Appendix 1A. This incorporates all the additional calls identified as part of the October Budget Review. It assumes that the £0.711m of pressures identified earlier can be contained by corrective action in 2009/10 and, where costs continue, each year thereafter.

3.10 Total reserves are projected to fall from £21.2m to £10.4m by the end of 2012/13 as they are applied for earmarked purposes. Of this figure general balances are still above the minimum requirement of £6m (once the effect of IFRS accounting changes is taken into account in 2010/11); others are required for identified purposes. Balances are therefore projected to reduce rapidly and it will soon be unaffordable to support BSF from this source. It is essential that we determine how these costs can be mainstreamed to on-going funding sources for the future.

3.11 However the projection at appendix 1A does not factor in the full potential impact of recession. If this continues through 2010/11 at a similar level as 2009/10 then general fund balances will be needed to offset income shortfalls in the property trading account: by a further £0.6m in 2010/11 and perhaps 2011/12 as well. For this and other revenue pressures there is a £0.5m one year contingency for recession issues in 2010/11, reducing to £0.25m on 2011/12 and to nil thereafter. This provides some cover for continuing problems with income, but would only meet a proportion of what is required.

3.12 A failure to deliver on the current financial plan can only exacerbate the rapid approach of public spending constraint. It is becoming clear that all parties at the national level are now likely to make spending cuts in 2010/11. It is unlikely that local government will be exempt.

Capital

3.13 The 2009/13 capital programme currently plans spending of £70m (2009/10), £85m (2010/11), £52m (2011/12) and £23m (2012/13). This scale of spending is significantly above the level of recent years and includes three major investments: BSF, the Sports Academy (the Pods) and Baths Hall.

3.14 The 2009/13 programme is financed by a mix of grant, capital receipts and borrowing. Grant funding has now been confirmed for the first phase of BSF and for the Pods. However the availability of internal resources has changed since the budget was set and we need to consider whether the current programme as a whole is still affordable. In particular the projected timing and scale of capital receipts required by the programme has changed:

- The receipt for the town centre redevelopment is no longer expected in the programme period as the developer has deferred its plans for this investment (net £5m)
- Right to buy sales of former council houses have fallen dramatically and are forecast to undershoot budget projections by £1.3m over the same period.

3.15 There are a number of options:

- To reduce or delay spending so that it matches the available funding profile
- To identify alternative capital receipts from the sale of other assets
- To change the funding mix by increased prudential borrowing which would require additional revenue savings to meet the cost of financing additional debt

3.16 In making a choice, affordability and value for money considerations are key. A combination of the options is proposed, which will need to be pursued vigorously to close the current funding gap:

- It is in the nature of capital scheme planning that at times the original timetable has to be revised because of funding delays, planning requirements or other logistical issues. This produces a natural delay in spending as reported below
- This should be reinforced by establishing a formal process for approval before letting new contracts (for example by reference to the leader and chief executive)
- A rigorous review of other asset disposal options should be made to substitute for those now delayed
- A search for radical revenue efficiencies would also provide the scope to finance an increase in prudential borrowing.

3.17 At this stage there is forecast slippage in the capital programme of £9.7m from 2009/10 to 2010/11. Of this only £0.9m is internally funded. There are also additional costs of £0.4m on BSF procurement and Normanby Enterprise Park reclamation. Cabinet are invited to approve these costs and rephasing (see Appendix 2), Further reviews will be made later in the year.

Efficiency savings

3.18 For the period 2008/11 government has set an ambitious target of 10% efficiency savings for public sector bodies. In the case of local government the savings remain with the local authority, but must represent real cashable savings.

3.19 For North Lincolnshire Council the 10% target equates to £15.3m an increase on the original 9% figure of £13.6m. Although the council comfortably achieved the 7.5% target for 2005/08 it has made a slow start against the new target. It achieved savings of £2.4m in 2008/09 and on current plans will make a cumulative total of £7.4m efficiency savings by 2010/11, a shortfall of £7.9m (see appendix 3).The council is required to confirm its target for 2009/10 by October 2009. It is proposed that a target of £2.28m is set.

3.20 The ground still to be made up reinforces the need to accelerate the council's strategic transformation programme. A start has been made with the 'Worksmart' project reviewing the council's office accommodation portfolio and how it is used. It is proposed that the efficiency agenda is vigorously pursued to achieve a number of objectives:

- To help meet current recessionary pressures without impacting on service delivery
- To secure delivery of the council's capital investment priorities
- To achieve the efficiency targets set for the public sector and demonstrate our commitment to providing value for money
- To position the council well for the radical reappraisal of public expenditure expected after the next election. In particular

savings which can be made now or in 2010/11 will lessen the impact of transition to the harsher financial climate.

The council therefore needs to consider all options for more efficient working to put it on a stable financial footing for the future.

Treasury

3.21 The recent crisis in world financial markets has made finding a secure home for surplus cash difficult. The action taken by governments to deal with the crisis, including an aggressive reduction in central bank base rates, has also significantly impaired our ability to secure a decent return on cash invested.

3.22 In setting the budget for 2009/10 the target return on investment was reduced from £2m to £0.5m, with the emphasis on maximising security at the expense of return. Only UK institutions with high credit ratings and backed by the government credit guarantee scheme are being used. There is a projected shortfall of £0.15m in 2009/10, but this can be mitigated by extending the maximum investment term from one to three months. This is in line with the approved strategy and can be justified in the light of increased market stability over the past six months. The recent investment position is shown at appendix 4.

3.23 The council's borrowing strategy is to borrow only to support the capital programme. However while the relative cost of borrowing (interest rates of 4.5%) significantly exceeds the return on investment this borrowing has been deferred. Cash in hand is being used to fund capital spending in the short term which reduces cash balances at risk in the markets at the same time as providing a financial benefit. The savings made are expected to offset the shortfall on interest earned. The policy will be kept under review to respond to any adverse movements in long-term interest rates.

3.24 Total council debt at 31 March 2009 was £118.959m. At this point borrowing of £6.3m to support the 2008/09 programme and £11.7m planned for 2009/10 has been deferred.

4. ANALYSIS OF OPTIONS

4.1 These are considered in section 3.

5. RESOURCE IMPLICATIONS

5.1 Financial implications are considered in section 3. The impact on staffing, the property portfolio and IT resources will depend on specific decisions taken to address budget shortfalls and the efficiency agenda.

6. OTHER IMPLICATIONS

6.1 The risk of a budget overspend is addressed by the proposals made in this paper.

7. OUTCOMES OF CONSULTATION

7.1 Not applicable

8. RECOMMENDATIONS

8.1 That earmarked reserves and contingency funds are applied as follows:

- £0.500m of contingency to offset the impact of recession (para 3.2)
- £0.725m of earmarked reserves to meet additional costs on BSF and waste procurement, and the property trading account (para 3.3)
- £0.166m of contingency to meet fuel cost inflation (para 3.5)

8.2 That services provide clear action plans to contain the balance of £0.711m other cost pressures within approved budgets (para 3.6)

8.3 That the amendments to the capital programme identified in Appendix 2 be approved

8.4 That to ensure capital programme affordability:

- A formal process is established to seek approval from the leader before new contracts are let
- A rigorous review of asset disposal options is made to substitute for those now delayed
- A search is made for radical revenue efficiencies to provide scope to finance an increase in prudential borrowing

8.5 That the efficiency savings target for 2009/10 is set at £2.28m

8.6 That the policy of accelerating the transformation programme is endorsed

8.7 That treasury performance for the year to date is noted.

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Background Papers used in the preparation of this report
'Quarterly Treasury Management and Strategy Report', Audit Committee 30 September 2009

REVENUE FORECAST 2009/10 **APPENDIX 1**

Service	Annual Budget	Forecast	<-------------------------Analysis of Forecast----------------------→				
		Over (+)/ under(-) budget	Recession impact on General Fund	Additional call on earmarked reserves	Call on fuel contingency	One year pressures/ savings	Base pressures/ savings
	£'000	£'000	£'000	£'000	£000	£'000	£000
Neighbourhood & Environment	17,270	**590**	220	300		70	
Asset Management & Culture	8,400	**357**	251				106
Highways & Planning	8,946	**376**	277		166	-67	
Community Planning & Resources	6,304	**284**					284
Children & Young Peoples Service	28,810	**279**		279			
Corporate Budgets	7,699	**70**				70	
Adult Social Care	35,115	**0**					
Central Budgets	13,990	**0**					
Finance	4,314	**0**					
Human Resources	1,910	**0**					
Legal & Democratic	2,828	**0**					
Commercial Units							
Property Trading Account	-1,996	**171**		171			
Building Control	0	**-25**		-25			
General Fund total	133,590	**2,102**	748	725	166	73	390
Recession and fuel contingency applied		**-666**	-500		-166		
Net total		**1,436**	248	725	0	73	390
Use of earmarked reserves		**-725**		-725			
Balance of cost pressure on general fund (para 3.6)		**711**	**248**	**0**	**0**	**73**	**390**

COMMENTARY **APPENDIX 1 Continued**

At the end of period 5 services are reporting pressures of £2.1m, £1.4m after the use of contingency. The issues are:

- Neighbourhood & Environment are reporting a projected overspend of £590k. This include additional Waste Procurement project costs, reduced income from Schools catering and licensing and bad debt write-offs relating to the homeless rent bonds.

- Asset Management & Culture have highlighted pressures of £357k. The recession has affected income recovery from sports and leisure facilities and there are significant pressures on accommodation costs.

- Highways & Planning are forecasting a pressure of £376k. This relates to the underachievement of income from car parking, capital fee income and planning applications. In addition there are cost pressures relating to street lighting energy costs.

- Community Planning & Resource are forecasting an overspend of £284k due to difficulties in achieving budgeted efficiency savings within Customer Services and the Business Transformation divisions. Also the Reprographics Unit are currently underachieving on income.

- The Children & Young Peoples Service are projecting an overspend of £279k relating to Building Schools for the Future.

- Corporate Services have highlighted a budget pressure of £70k relating to staffing costs on the Acorns Neighbourhood Management project.

- In addition the Property Trading Account is forecasting a significant loss from reduced income and increased costs in managing their commercial properties. This is expected to take up the whole of its reserve. The budget assumed £400k use of PTA reserves with the PTA going into deficit in 2010/11: this forecast takes all £572k.

- Building Control is expected to make a call of £100k on its reserve compared to £125k budgeted. There is no revenue impact in 2009/10, but the reserve is expected to be fully utilised by the end of 2010/11.

APPENDIX 1A

RESERVES	2008/09 Closing Balance Actual £'000	2009/10 Closing Balance Estimated £'000	2010/11 Closing Balance Estimated £'000	2011/12 Closing Balance Estimated £'000	2012/13 Closing Balance Estimated £'000
General Reserves					
General Fund	(6,858)	(6,858)	(6,358)	(6,358)	(6,358)
Collection Fund	(1,301)	(708)	(500)	(500)	(500)
Schools Balances	(2,246)	(1,846)	(1,852)	(1,652)	(1,452)
Earmarked Reserves					
Revenue account support	(4,081)	(2,724)	(1,857)	(1,256)	(655)
Insurance Reserve	(1,000)	(1,000)	(1,000)	(1,000)	(1,000)
Insurance Fund Profit/Loss	(238)	(238)	(238)	(238)	(238)
PTA Revenue Reserve	(572)	0	0	0	(110)
HRA Closure Reserve	(125)	0	0	0	0
Corporate Reserve	(30)	(30)	0	0	0
Crematorium enhancement	(37)	(28)	(30)	(32)	(34)
Dedicated Schools Grant	0	0	0	0	0
NLH Pumping Station	(21)	(26)	(31)	(36)	(41)
Carry Forwards	(583)	0	0	0	0
Building Control P&L	(231)	(131)	0	0	(20)
Investment Impairment	(2,853)	(2,853)	0	0	0
PRG Reserve	(576)	(288)	0	0	0
MRP Reserve	(460)	(460)	(460)	(460)	0
Scunthorpe Special Expenses	(6)	(6)	(6)	(6)	(6)
REVENUE RESOURCES	**(21,218)**	**(17,196)**	**(12,332)**	**(11,538)**	**(10,414)**

CAPITAL PROGRAMME CHANGES 2009/10 **APPENDIX 2**

	Total	Grant	Internal
	£000	**£000**	**£000**
Increase in cost in 2009/10			
BSF Procurement	293		293
Schools sustainability initiative	13		13
Normanby Enterprise Park	110		110
Sub-total	**416**		**416**
Reduction in budget 2009/10			
Sub regional housing project	-850	-850	
Sub-total	**-850**	**-850**	
Rephase to 2010/11			
BSF Construction	6,343	6,205	138
The Pods (Sports Academy)	2,329	1,946	383
Safety Camera Partnership	38	38	
Manifold Road Project	400	275	125
Foxhills Sports Football Facility	250		250
Property trading account Plot 12 , Normanby	82	82	
Property trading account Plot 25 , Normanby	267	267	
Sub-total	**9,709**	**8,813**	**896**

COMMENTARY

Increase in costs

Building Schools for the Future procurement (forecast £293k overspend). Delays in the delivery of financial closure and the anticipated requirements of the next phase of dialogue suggest there will be an overspend on the scheme in 2009/10. This will need to be further reviewed for phase 2 and 3 implementation plans.

Schools Sustainability Initiative (overspend of £13k). This should have been accrued in 2008/09 as the scheme is complete.

Normanby Enterprise Park (forecast £110k overspend). A dispute with the contractor used on Normanby Enterprise Park Phase 5 has now been resolved, with the result that the council must pay an additional £110k of costs. The contractor has subsequently made a further claim for an additional £297k which is still subject to adjudication. Additional funding is required at this stage to meet the £110k overspend.

Reduction in budget

Sub-regional Housing Project (£850k correction). The Council’s funding allocation wrongly included an amount that should have been designated for the East Riding of Yorkshire Council. The project budget is to be corrected and funding transferred.

Rephasing from 2009/10 to 2010/11

The BSF construction programme is now under way at Brumby Technology College. However financial close for the first two schools took longer than planned. There have been further delays with the Melior College scheme as planning and funding issues are resolved (forecast £6,343k slippage).

The Pods (Sports Academy) (forecast £2.329m slippage). This is due to a delayed start on the scheme as funding from Yorkshire Forward was confirmed.

Manifold Road Showman & Travellers project (forecast £400k slippage). Tenders for work on the site are still to be placed and it now anticipated that the majority of the programme will be slipped into 2010/11.

Foxhills Sports & Football facilities (forecast £250k slippage). This project is linked to the BSF project and will now be delayed until 2010/11.

Safety Camera Partnership (forecast £38k slippage). The projected programme underspend has increased by £7k from the period 5.This scheme is a fully grant funded project and it is proposed that the underspend should slip into 2010/11.

Property Trading Account Developments (forecast £349k slippage). Normanby Enterprise Park plots 12 & 25 are now unlikely to commence development in 2009/10 and will slip into 2010/11

APPENDIX 3

EFFICIENCY TARGET 2008-11

Service Area	Service Efficiency target 2008-11 £'000	Cross cutting Efficiencies £'000	Target Service Efficiencies £'000	Value of On-going Efficiency Gain Achieved in 2008-09 £'000	Estimated Value of further Efficiency Gain to be Achieved in 2009-10 £'000	Estimated Value of Further Efficiency Gain to be Achieved in 2010-11 £'000	Estimated Cross cutting Efficiencies 2008-11 £'000	Total value of Efficiency gains identified 2008-11 £'000
Adult Social Care	4,235	185	**4,420**	754	373	346	120	**1,593**
Asset Management & Culture	927	247	**1,174**	53	519	190	160	**921**
Children & Young People	-			-				
-Children Strategy & Partnership	1,738	168	**1,906**	273	393	291	109	**1,066**
-Learning, Schools & Communities	1,688	107	**1,795**	172	91	1	69	**333**
Community Planning & Resources	635	126	**761**	288	245	198	81	**812**
Corporate Budgets	422	47	**469**	53	40	35	30	**158**
Finance	478	47	**525**	259	72	184	30	**546**
Highways & Planning	1,313	172	**1,485**	322	268	392	111	**1,093**
Human Resources	201	14	**215**	23	30	0	9	**62**
Legal & Democratic	262	33	**295**	4	0	0	21	**25**
Neighbourhood & Environment	2,060	284	**2,344**	218	249	165	184	**815**
Total	13,959	1,430	**15,389**	2,419	2,280	1,802	924	**7,425**

TREASURY INVESTMENTS **APPENDIX 4**

INVESTMENT POSITION 31 AUGUST 2009					
			£		
CALL ACCOUNT BALANCES					
	Abbey National Call Account		4,957,034		On call
	Bank of Scotland 7 Day Notice Account		2,708,327		On call
	NatWest Special Interest Bearing Account		8,671,271		On call
OTHER INVESTMENTS					
	Barclays Bank PLC		5,000,000		Repayment at term
	Debt Management Office		19,250,000		Repayment at term
	Heritable Bank Limited		2,935,588		In administration
	Landsbanki Islands		2,000,000		In receivership
TOTAL			**45,522,220**		