

## Appendix 1

### **Rossendale Borough Council Budget 2008/09 Risk Analysis and Report Under s25 of the Local Government Act 2000**

This analysis is produced in order to:

- a) Support the conclusions as to the robustness of the budget and adequacy of reserves set out in the Chief Finance Officers report under 25 of the Local Government Act 2000.
- b) Inform members of the financial risks facing the Council for consideration as part of their debates around the setting of the budget and approving the Medium Term Financial Strategy.

Financial risks are clearly of various sorts but can broadly be characterised as follows:

- The chance of overspending against budget
- The chance of underspending against budget
- The chance of an unforeseen event with a major financial impact (for example a flood or similar event)

Clearly such risks might have either a positive or negative effect on the Council's overall financial position and it is the purpose of the financial management process to allow the Council to both identify the risks it faces and the steps required to either mitigate them in the case of negative risks or exploit them in the case of positive risks.

Turning to the specific risk areas within the Council's budget for 2008/09 the following specific areas of risks have been identified.

<b>Expenditure/Income Heading</b>	<b>Impact</b>	<b>Likelihood</b>	<b>Comments</b>
<b>Employee Costs</b>			
Pay awards	Medium	Medium	The budget assumes 2.5% for pay awards for 2008/09 while initial claims is for 6% the Treasury guidelines is 2% and any awards will be in the context of what is a very light Local Government finance settlement. Given this there is a risk of service disruption due to strike action. A 1% variance equates to a c.£69k
Job Evaluation	High	Medium/High	The pay and grading structure proposed as a result of Job Evaluation depends for its affordability on the full implementation of a set of measures which provide some compensating savings. Elements of these measures have yet to be agreed and there therefore remains a risk of at least £40k. In addition the Trade Union side have not agreed the proposed pay and grading structure which results in significant risk in this area.
Vacancies	Medium	Certain	Vacancies will inevitably occur generating savings. No savings are assumed with base budget providing some cushion in relation to pay awards. Savings in previous years have been around £100k
Pension Contributions	High	Low	Contribution rates for the three years commencing 1.4.08 can be frozen at current levels. However, this assumes continued good investment performance and some positive benefit from scheme changes. An element of the stock transfer proceeds was earmarked to mitigate pension risks. However, elements of the transfer agreement need to be reengineered in order to facilitate to take into account the views of the District Auditor on the status of schemes payable under the Transfer Agreement. A requirement to provide for 1% additional contributions equates to £50k

<b>Expenditure/Income Heading</b>	<b>Impact</b>	<b>Likelihood</b>	<b>Comments</b>
<b>Running Costs</b>			
Energy and Fuel	Medium	High	Prices in the international fuel and energy markets are currently highly volatile. Additional inflationary provision has been made in 2008/09 and in future forecasts. However, energy contracts will need to be retendered during the forecast period and it is possible given the recent market movements that tendered prices may be in excess of budgets. This is a particularly volatile area but previous overspends have been contained within the overall budget. A 10% variation which is possible equates to £35k
Repairs and maintenance	Medium	Medium/High	This area of the budget has consistently overspent in the past and is highly demand driven. While the availability of resources in the capital maintenance programme will reduce demand over time the tipping point has yet to be reached. A variance of 10% equates to £23k.
Insurance	Medium	Medium	The Council's insurance contract needs to be relet during this planning period. The pool of providers of local authority insurance is very small and it is likely costs will increase by more than inflation a fact reflected in financial forecasts. Much of the Council's investment programme is aimed at reducing exposure to insurable risks and this is a factor which will be reflected in the procurement process A 5% variance which is within the forecast range equates to £11k
<b>Contract Costs</b>			
ICT	Low/Medium	High	The Council has been going through a process of successfully negotiating down the costs of the ICT contract. This will continue but while further reductions will occur they are likely only to be on a relatively small scale until it is necessary to retender
Leisure	High	Medium/High	The two leisure trusts are affected to a significant extent by movements in energy prices and while to 2008/09 budget injects significant additional

Expenditure/Income Heading	Impact	Likelihood	Comments
			resources to the two trusts trading margins and the strength of balance sheets remain fragile. The ability of the Trusts to raise prices is also constrained by market conditions. While there is little direct competitive pressure there is now direct competition to Ski Rossendale which is a major income generator. The opening of the new Haslingden Lifestyle Centre may ease the position in due course. While contract prices are fixed the Council cannot be wholly insulated from the trading position of the Trusts and may face calls for additional resources. A 5% variation due to increased energy costs for instance would equate to £33k on its own. Total risk including the possibility of emergency building works needs to be seen as at least £100k.
Revenues Benefits and Customer Contracts	Low	Low	The price of this contract is linked to RPI and while this index is increasing it is foreseeable. As the contract price is fixed the risk of non-inflationary variations is slight. The contract does contain an incentivisation mechanism which will generate rewards to the contractor. However, this mechanism is capped and reserves to meet roughly three years payments under this mechanism have already been set aside.
Housing Benefits	Very High	Medium/High	Expenditure in this area at some £16m is the largest single item of expenditure in the Council's budget. While this expenditure is fully funded by grant there is an extremely complex system of rules that determine what is and what is not eligible for grant. Variations are likely in particular in relation to the recovery of overpayments and change to the benefit rules from April 2008, may increase the risk of overpayments being made. Given that a 1% variance on this budget amounts to £160k the changes from April 2008 and the previous history of variances in this area significant caution needs to be exercised in this

Expenditure/Income Heading	Impact	Likelihood	Comments
			area
Concessionary Fares	High	High	<p>Given the changes from April 2008 this has to be regarded as a very high risk budget. Given the elements of uncertainty and factors in the changes to the scheme which would seem to favour the Council the budget has not been increased to reflect the overspend in the current year (£100k). Should an overspend of this nature recur significant resources will be available in the budget volatility reserve. A 1% variance in this area amounts to £10k, however the estimates made by consultants in relation to the April 2006 changes were out by some 30% illustrating how volatile this area of spending is. Based on this financial risk needs to be seen as in the range +/- 10%, or £100k.</p> <p>In order to mitigate this risk to the above levels it is proposed that the Council joins forces with the other Lancashire Transport Authorities (ie the District &amp; Unitary Councils) in a pooling arrangement the object of which is to mitigate individual local authority exposure.</p>
<b>Income</b>			
Planning Fees	Medium	Medium/High	<p>This budget is subject to the impact of changes in the wider economy with a slow down in the economy likely to lead to a slow down in applications coming forward, particularly major applications. The budget has not been increased to reflect current levels of activity and while the Government has proposed fee increases the level of these has not been confirmed and they have not been reflected in the budget. In addition these increases will be accompanied by other changes which will reduce the numbers of applications on which fees can be charged. The effect of this charge can not be quantified at present. This prudent approach should serve to mitigate the apparent risk. A 10%</p>

Expenditure/Income Heading	Impact	Likelihood	Comments
			variance which is wholly possible in this area amounts to £30k
Building Control Fees	Medium	Medium	Similar factors impact on this budget as apply to planning fees, although fees are set locally. This service continues to trade effectively and historically has managed to maintain its position. A 10% variance in this area amounts to £18k
Market Rents	Medium	High	Market rents have failed to achieve budget consistently in recent years. This pattern reflects changes in shopping patterns and economic forces which are beyond the Council's control. While the budget has been adjusted to a more realistic level there still remains a risk in the +/- 10% range equality to £12k
Capital Financing and Interest	High	High	This budget is driven by both the level of interest rates and the level of cash available for investment. The Council utilises the service of Treasury Management Advisers to assist with interest rate forecasts, and cash flow forecast are updated on a regular basis in light of actual patterns of receipts and payments. This remains a highly volatile budget due to the inability to influence interest rates and the difficulties in prudent forecasting cashflows, although assumptions are used. The risk is in the range +/- 15% or £36k

In Summary this gives risks in the revenue budget in the range below

	<b>Worst Case £000</b>	<b>Best Case £000</b>	<b>Weighted Average £000</b>
Pay awards	60	0	30
Job Evaluation	40	0	0
Staff Vacancies	0	-100	0
Pension Contributions	0	0	0
Energy and Fuel	35	0	35
Repairs and Maintenance	23	0	23
Insurance	11	-11	0
ICT Contract	0	0	0
Leisure Contracts	100	0	100
Revenues, Benefits and Customer Contract	0	0	0
Housing Budget Payments	160	160	80
Concessionary Fares	100	100	100
Planning Fees	30	-30	0
Building Control	18	-18	0
Market rents	12	0	12
Capital Financing and Interest	36	-36	36
<b>Total</b>	<b>602</b>	<b>65</b>	<b>416</b>

The implication of this range of possible variations is that on a worst case basis the Council needs to maintain reserves of at least £602k to set against the identified risks.

### **Conclusion and Adequacy of Reserves**

Having considered the exposure to risk the following shows how this risk relates to the Council's reserves:

	<b>£000</b>
Maximum Financial Risk Exposure	602
Minimum level of General risk	500
	1,102
Less est General Reserve @ 31.3.08	750
est Budget Volatility Reserve @ 31.3.08	<u>143</u>
Notional shortfall in available reserves	<u>209</u>

However, it is unlikely that all these risks will materialise at once, and if the worst case possible variation is adjusted for likelihood set out in the risk assessment then the following shows the requirement to maintain reserves

	<b>£000</b>
Weighted Financial Risk Exposure	416
Minimum Level of General Reserve	500
	916
Less est General Reserve at 31.3.08	750
Est Budget Volatility Reserve at 31.3.08	<u>143</u>
Notional short fall in reserves	<u>23</u>

This notional shortfall equates to 2.7% of forecast reserve and 0.2% of the likely budget requirement for 2008/09. In this context it is not material and it is likely that such a shortfall could be managed within routine variations to the budget.

Therefore, no budget is without some exposure to risk. However, the position in Rossendale is such that risks have been identified and either provided against or the above considered view taken that the scale of them is manageable.

The degree of risk that remains evident in the budget influences the view which should be taken on the level of reserves which the Council need to maintain, which is the second strand to this statutory advice. The Council's financial strategy suggest that Members consider a target range for general reserves of £0.5-£0.75m. General reserves as at 1st April 2007 were £750k and are expected to remain at this level as at 31<sup>st</sup> March 2008. The above "notional" shortfall demonstrates that general reserves should be maintained at the level of £750k. This level of general reserves, together with other smaller earmarked reserves, will allow a cushion against the sort of risk which have been identified and those unforeseen incident which may from time to time arise. The Medium Term Financial Strategy includes a forecast of all reserves over the medium term.

Therefore in conclusion I am able to give positive assurance to Members as to:

- The adequacy of General and earmarked reserves to address the risks against which they are held and
- The robustness of the budget for 2008/09.

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