FINANCIAL STABILITY

Government Grant Funding of Local Expenditure

1. Cheshire East receives two main types of Government grants, formula grant and specific grants. The overall total of Government grant estimated for 2011/2012 was £419.0m.

2. In 2011/2012 Cheshire East Council's formula grant was £70.3m and specific grants were budgeted to be £373.8m based on Government announcements to February 2011. Further announcements revised this figure to £348.6m. Specific grants are split between non-ringfenced (£128.7m) and ringfenced (£219.9m). Spending in relation to ringfenced grants must be in line with the purpose for which it is provided.

3. The table below is a summary of the budgeted and updated position for all grants in 2011/2012. A full list of grants is provided at Annex 1, Appendix 1.

Table 1 – Summary of Grants to date

	Original Budget 2011/12 £m	Revised Budget 2011/12 £m	Cash Received 2011/12 £m	Variance from revised budget to cash received 2011/12 £m
Formula Grant				
Revenue Support Grant	16.6	16.6	16.6	0.0
Business Rates	53.7	53.7	53.7	0.0
Specific				
Ringfenced Grants	248.1	219.9	219.9	0.0
Non Ringfenced Grants - held within service	95.5	95.5	101.1	5.5
Non Ringfenced Grants - held corporately	30.2	33.2	32.7	(0.5)
Total Government Grant Funding	**444.1**	**419.0**	**424.0**	**5.0**

Source: Cheshire East Finance

4. Various unconditional non-ringfenced grants have been received during the last quarter of 2011/2012. Accounting rules now require these corporately held grants to be credited to the revenue account, and therefore are effectively held in year-end general reserves. As some of these were received too late for services to seek approval to spend against in 2011/2012, services will be requesting Supplementary Estimates for £75k in 2012/2013 to enable them to utilise these funds.

5. Overall since TQR there has been a decrease in ringfenced grants of £542k. At TQR it had been assumed that £0.8m additional grant (after approved allocations to services) would be added to balances. However, at outturn this figure has reduced to £0.2m mainly as a result of four small Children and Families grants that are now not expected to be received, and retrospectively claimed grants which have been reflected in service outturn positions.

Collecting Local Taxes for Local Expenditure

6. Cheshire East Council collects Council Tax and National Non Domestic Rates (NNDR) for use locally and nationally.

Council Tax

7. Council Tax is set locally and retained for spending locally. Council Tax was frozen for 2011/2012 at £1,216.34 for a Band D property. This is applied to the tax base.

8. The taxbase for Cheshire East reflects the equivalent number of domestic properties in Band D that the Council is able to collect Council Tax from (after adjustments for relevant discounts, exemptions and an element of non collection). The taxbase for 2011/2012 was agreed at 146,899.21 which, when multiplied by the Band D charge, means that the expected income for the year is £178.7m.

9. In addition to this, Cheshire East Council collects Council Tax on behalf of the Cheshire Police Authority, the Cheshire Fire Authority and Parish Councils. Table 2 (below) shows these amounts separately, giving a total collectable amount of £213.1m.

Table 2 – The majority of Council Tax is retained by Cheshire East

	£m
Cheshire East Council	178.7
Cheshire Police Authority	21.2
Cheshire Fire Authority	9.8
Town & Parish Councils	3.4
	213.1

Source: Cheshire East Finance, Sept 2011

10. This figure may vary slightly during the year if more discounts and exemptions are granted or more properties are built.

11. The Council expects to collect at least 99% of the amount billed, but will always pursue 100% collection. However, to allow for any delay in collection the amount billed should therefore be slightly more than the actual budget. The amount billed to date is £213.7m.

12. Table 3 (below) shows collection rates for the last three years, and demonstrates that 99% collection is being achieved within three years.

Table 3 – 99% of Council Tax is collected within 3 Years

	% Collected to date
2009/2010	99.2%
2010/2011	98.8%
2011/2012	97.9%

Source: Cheshire East Finance, May 2012

National Non Domestic Rates (NNDR)

13. NNDR is collected from businesses in Cheshire East based on commercial rateable property values and a nationally set multiplier. The multiplier changes in line with inflation and takes account of the costs of small business rate relief. The inflation factor used is 4.6% which reflects the Retail Price Index as at September 2010. NNDR is set nationally and paid over into the NNDR pool to be re-allocated across the country according to need.

14. The small business multiplier applied to businesses who qualify for the small business relief has been set at 42.6p in 2011/2012. The non-domestic multiplier has been set at 43.3p in the pound for 2011/2012.

15. The amount collected does not relate to the amount that is redistributed to the Council but it must be noted that the total collected includes amounts that will be distributed to police and fire authorities as well as local government.

16. Table 4 (below) demonstrates how collection continues to improve even after year end. The table shows how over 99% of non-domestic rates are collected within three years.

Table 4 – Over 99% of Rates are collected within 3 years

	% Collected to date
2009/2010	99.7%
2010/2011	99.1%
2011/2012	98.1%

Source: Cheshire East Finance, May 2012

Central Adjustments

Capital Financing Costs

17. The capital financing budget includes the amount charged in respect of the repayment of outstanding debt and the amount of interest payable on the Council's portfolio of long term loans. These budgeted costs are partly offset by the interest the Council anticipates earning from temporary investment of its cash balances during the year.

18. At TQR, the overall saving on the capital financing budget was forecast to be £0.7m. At outturn this has risen to £1.7m, as a result of a £1m underspend on debt repayments due to slippage in the capital programme, and £0.7m savings in external interest costs.

Treasury Management

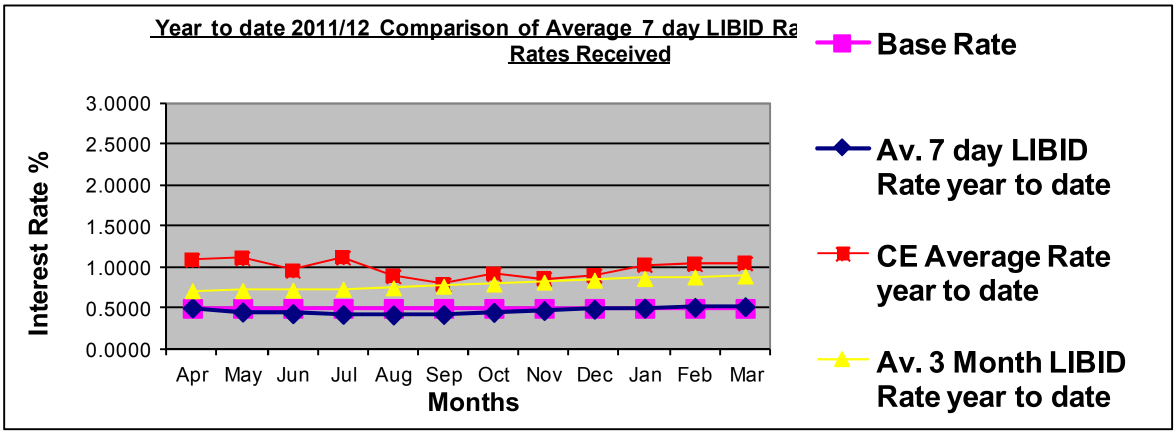
19. Investment income received in 2011/2012 was £816,000, slightly higher than the budget of £800,000:

Source of Income	£
In House Managed Investments	603,000
Fund Manager Interest	139,000
Heritable Bank in Administration	63,000
Other	11,000
TOTAL	**816,000**

- The average lend position (the 'cash balance') including fund manager in the year was £70.5m.
- The average interest rate received on in house investments in the year was 1.12%
- The average interest rate received on the externally managed pooled funds in the year was 0.83% (0.56% after fees).

20. The Council's total average interest rate in the year was 1.05%. This is favourable when compared to the London Inter-bank Bid Rate for 7 days at 0.52%. The base rate has remained at 0.50% for the quarter.

Comparator	Average Rate Q4
Cheshire East	1.05%
LIBID 7 Day Rate	0.52%
LIBID 3 Month Rate	0.89%
Base Rate	0.50%



Counterparty Limits and Investment Strategy

21. The maximum amount that can be invested with any one organisation is set in the Treasury Management Strategy Report. For named UK banks, UK building societies and foreign banks this has been set as 15% of our total investments, subject to a maximum value of £15m. These limits apply to the banking group that each bank

belongs to. The Council did not invest directly with any foreign banks during 2011/2012.

22. The maximum amount that can be invested with any Money Market Fund has been set at 25% of our total investments subject to a maximum value of £20m. There is also a maximum that can be invested in all Money Market Funds at any one time of 50% of the value of all investments.

23. During 2011/2012 all UK banks have had their credit ratings reviewed mainly as a response to the ongoing debt crisis in the Eurozone. A number of banks which the Council had been using for investment purposes were downgraded and now fall below our minimum investment criteria. Cheshire East has only invested with UK institutions and money market funds. The table below shows the limits relating to each organisation and the investments as at 31st March 2012. Where counterparties have been removed from our list then no new investments are being placed and funds already with those institutions are being recalled in line with the terms of the investments.

Counterparties	Limits		Investments as at 31/03/12	
UK BANKS				
Barclays Bank	15%	£15m	-	-
Co-operative Bank:	15%	£15m	-	-
HSBC Bank	15%	£15m	-	-
Lloyds TSB	15%	£15m	6%	£3m
Royal Bank of Scotland	15%	£15m	10%	£5m
Santander (UK) plc	15%	£15m	10%	£5m
Standard Chartered Bank	15%	£15m	-	-
Monet Market Funds	50%		34%	
Deutsche	25%	£20m	8%	£4m
Ignis	25%	£20m	9%	£4.5m
Prime Rate	25%	£20m	10%	£5m
Scottish Widows	25%	£20m	7%	£3.6m
Pooled Funds - External Fund Manager	50%		40%	£20m
				£50.1m

24. With the ongoing crisis in the financial system, particularly within the Eurozone, all financial institutions and Money Market Funds are subject to ongoing monitoring by the Council's Treasury advisors, Arlingclose. The Council can react to concerns over any institutions that are on the approved list to ensure that any risk to the Council is minimized. The Council is currently limiting the duration of any new investments to allow for quicker reaction to market changes. The effect of removing counterparties from the lending list and limiting the duration of new investments will reduce the amount of interest received from future investments

Performance of Fund Manager

25. The table below shows the performance of the funds (net of fees) since the initial investment of £20m (£10m in each model) on 27th May 2011.

	STANDARD MODEL	**DYNAMIC MODEL**
June 2011	-0.04%	-0.13%
July 2011	0.21%	0.23%
August 2011	-0.17%	-0.47%
September 2011	-0.09%	-0.24%
October 2011	0.16%	0.28%
November 2011	-0.07%	-0.19%
December 2011	0.09%	0.12%
January 2012	0.39%	0.46%
February 2012	0.05%	0.10%
March 2012	0.10%	0.15%
Cumulative since start	0.64%	0.31%
Value of Investment at 31/03/12	£10,085,046	£10,053,946
Fees	£21,220	£22,840
Annual Equivalent Rate as at 31/03/12	0.75%	0.37%

26. Since the last quarter the funds have shown a marked improvement although weakening financial markets caused by worries on the Greek and Spanish economies has reversed some of these gains at the start of 2012/2013.

27. Market sentiment whether based on fact or rumour, will continue to affect performance which could easily see large swings both upwards and downwards. Most of the increased value to the funds has been attributable to emerging markets debt where economies are not currently affected by the recessionary worries of Europe and the USA. It was poor data coming from the USA economy and the escalation of the Greek debt crisis that led to poor fund performance in August and September.

28. Whilst the performance of the fund since the Council joined is not as good as originally hoped, these investments should be seen as a longer term investment so true performance can only be judged over a longer period of time.

Borrowings

29. The Council currently has debt outstanding of £132.3m of which £115.3m is from the PWLB and £17m is in the form of market LOBO loans. The only borrowing activity which took place in 2011/2012 was to refinance £5m maturing PWLB debt with a new 10 year PWLB Equal Instalments of Principal (EIP) loan at a rate of 2.09%. Whilst there is a short term cost of carrying this loan (compared to investment rates)

this does offset the interest risk inherent in waiting until liquidity issues force new borrowing.

30. The maturing debt arose out of a £50m debt restructuring exercise in July 2010 which assumed savings of £4.47m over 10 years based on refinancing the debt at 4.22%. As the refinancing in 2011/2012 did not take place until March and was at the lower rate of 2.09% then savings are forecast to be higher. Budgeted savings from debt restructuring up to 31/03/12 were £1.4m, although actual savings are £1.6m.

Treasury Management Advisors

31. The contract for provision of Treasury Management advice expired on 31st December 2011. Following a tendering process, Arlingclose Ltd were re-appointed to provide treasury advice for another 3 years.

Central Contingencies

Pay, Prices and Pensions Inflation

32. The 2011/2012 budget contained £2.1m contingency provision to meet the potential impact of general inflation on service budgets, and to meet estimated costs of increases in Employer National Insurance and Pensions contributions. This was fully allocated to services, and is therefore reflected in service outturn positions.

Severance and relocation costs

33. A provision of £4.167m was included in the 2011/2012 budget to meet ongoing actuarial charges relating to Voluntary Redundancies (VR), and relocation costs arising from Local Government Reorganisation. Actuarial costs of £3.917m, and relocation costs of £0.545m were incurred in 2011/2012, which in total exceeded the provision by £0.3m. Overall though, relocation costs are lower than originally forecast, and consequently provision has been made in the 2012/2013 budget to return surplus funding of £0.5m transferred to the Council on reorganisation.

Supplementary Revenue Approvals

34. The VR scheme has continued in 2011/2012 but costs are now funded by individual services rather than from a corporate reserve, and costs have been reflected in services' forecast outturn positions. However, as advised at TQR, the Council received approval to capitalise the statutory element of VR payments in 2011/2012, which has been prudently funded from the Capital Reserve rather than borrowing, with a resultant reduction in the impact on revenue budgets. Consequently service costs have been reduced by the capitalisation of VR costs of £2.3m.

35. At TQR, Council approved a Supplementary Revenue Estimate (SRE) of £0.6m (after capitalisation) to be funded from general reserves for one-off VR costs relating to ICT Shared Service and Adults Transport staff. However actual net costs of the VR payments in 2011/2012 were only £130k, as a result of the phasing of some leavers into 2012/2013, thereby reducing the impact on balances by £470k. VR costs in 2012/2013 will be met from the pump priming budget provision, and

therefore there is no need to earmark the remainder of the SRE approval as a call on reserves.

36. At Mid Year Review (MYR), Members also approved an SRE of £860k for Pay Harmonisation costs. Due to timing, only £261k was incurred and allocated to services in year, and therefore it is proposed that the balance of £599k be transferred to an earmarked reserve for drawdown in 2012/2013.

PFI costs

37. Following the Government's abandonment of the PFI schemes relating to Waste and Round 5 Extra Care Housing, it is necessary to write off costs of £1.7m previously treated as capital expenditure on these schemes to the revenue account. The Council did apply for a "capitalisation direction" – i.e. permission to continue to treat those costs as capital expenditure. However in a letter from the Communities & Local Government (CLG) Department dated 23 May 2012, the application was refused, on the grounds that (a) the expenditure was not unavoidable, and (b) there would not be unacceptable adverse impact on those who use or pay for services if the expenditure is met from revenue resources; i.e. the Department was not satisfied that meeting the PFI costs from revenue resources would cause exceptional financial difficulties for Cheshire East.

38. Whilst we are able to make another capitalisation bid in 2012/2013, in the light of the timing of our decision not to proceed with the project (April 2012) and also CLG's response in May, it is considered prudent to reflect the write off (£1.6m expenditure relating to the Waste PFI scheme, and £0.1m relating to the Extra Care Housing scheme) in the 2011/2012 accounts.

Other

39. Other miscellaneous items of income and expenditure including corporate write offs have contributed to a charge against balances of £0.2m.

Outturn Impact

40. The impact of the service outturn position (after capitalisation of VR costs of £2.3m) is to reduce balances by £8.2m. This is reported on fully in Annex 2.

41. Taken into account with the service related items detailed above, the impact of these service outturn issues is to reduce balances by £9.5m, summarised as follows:

	£m
Service Outturn	- 8.2
Capital financing	1.7
Grants	0.2
Relocation	- 0.3
SREs	- 1.0
PFI costs	- 1.7
Other	- 0.2
Total	- 9.5

Management of Council Reserves

42. As previously reported, the opening balance at 1 April 2011 on the Council's General Reserves increased from a projected £6.7m to an actual position of £12.5m, due to the improved outturn position for 2010/2011.

43. The Council's Reserves Strategy 2011/2014 stated that the Council would maintain reserves to protect against risk and support investment. The Strategy forecast an increase in the level of reserves to £15m by 31st March 2012 with a risk assessed minimum level of £14.7m.

44. Planned returns to reserves of £8.3m at MYR comprised a projected contribution from revenue funding of £5.1m, approved transfers of revenue earmarked reserves of £1.9m, VAT repayments of £1.1m (increased from the original estimate of £0.7m), and Business Financing scheme repayments of £0.2m, which increased to £0.3m at outturn resulting in a return to balances of £8.4m. At TQR a further £0.5m had been potentially identified for return to balances from the capital reserve, however after further investigation it has not been possible to release these monies.

45. Taken together with service outturn impacts above, the overall impact is a net reduction in general reserves of £1.1m to £11.4m as shown in Table 5 below.

Table 5 – Change in Reserves Position

	£m	£m
Opening Balance at 1 April 2011		12.5
Planned Contribution to reserves	5.1	
Fleming VAT claims	1.1	
Contribution from earmarked reserves	1.9	
Business Financing scheme	0.3	8.4
Service Outturn Impacts		-9.5
Closing Balance at 31 March		11.4

46. The balance of £11.4m is below the Reserves Strategy risk assessed minimal level of reserves of £14.7m, although it is in line with the £13.2m forecast at TQR. Further calls on the general reserve have been made which had been previously covered by the risk level of reserve. These comprised the Supplementary Revenue Estimates for pay harmonisation issues (£0.86m) and ICT Shared Service redundancies (£0.6m), and the charging of abortive PFI costs of £1.7m which have been prudently recognised against the 2011/2012 outturn position. The final general reserve position of £11.4m therefore remains adequate in risk terms.