

Committee(s): Finance Committee – For information	Date(s): 11/12/2018
Subject: Overview of contingencies and relationship to central risk budgets	Public
Report of: Chamberlain	For Decision
Report author: Philip Gregory, Deputy Director, Financial Services	

Summary

Finance Committee's practice on how to treat contingency requests has evolved over the last year. This report recommends a formalisation of that practice, so that departments and service committees requesting additional in-year funding are encouraged to manage within local risk budgets in so far as possible. It is proposed that contingency funding will only be allocated towards the end of the financial year when forecast year end positions are more accurate or in exceptional circumstances as outlined in paragraph 3. If contingency funding is not granted and a department overspends, the Finance Committee may waive the usual arrangements for clawing back the deficit from the following year's budget allocation.

Following a request from the Chairman of this Committee, this paper also sets out the purpose of central risk budgets, what they include and how they are managed including what options are available if unforeseen costs arise within this area. Central risk budgets generally cover strategically important income streams, corporate budgets or known volatile spend or income items, whereas contingencies are for unforeseen items of spend.

Recommendations

Members are asked to:

- Agree that departments should in the first instance seek to re-prioritise local risk budgets when unexpected pressures arise. And that any calls on the Finance Committee contingency should only be allocated towards the end of the financial year or in exceptional circumstances (see paragraph 3).
- Note the relationship between central risk and contingency arrangements, in particular that central risk budgets are for known volatile spend or income items; contingencies are for unforeseen items of spend.

Main Report

Background

1. At your September meeting, the Chairman requested a paper setting out how contingencies operate, the relationship with central risk budgets and what flexibility is available in these budgets to manage unforeseen costs.

Current Position

2. There are two contingency funds- a specific contingency fund for Policy and Resources Committee, with an annual allocation of £300k; and a contingency fund for the entire organisation held by Finance Committee, with an annual allocation of £1.8m. These annual sums are set aside to meet the costs of unforeseen and/or exceptional items that occur during the year, subject to approval by each Committee.
3. Financial Regulation 2.2 states that any deficit on the total of a Chief Officers local risk budgets is required to be carried forward and recovered from within the department's budget allocation for the following year, unless specifically waived by the Finance Committee. This arrangement may make departments and service committees reluctant to take the risk of trying to accommodate additional pressures within their local risk budgets; and encourage, therefore, requests for contingency funding.
4. The allocation of contingency funding depends upon the following criteria being met:
 - Contingency funding is only available for unforeseen items/events.
 - Officers should first assess whether costs can be funded within existing budgets.

Following Finance Committee decisions made earlier this year, two additional criteria are proposed for the use of Finance Committee's contingency:

- Requests relating to unforeseen events in the normal course of business are likely to be declined when made early in the year, as forecast outturn positions of allocated resources are likely to change during the financial year.
 - Requests may be made in year for clearly exceptional events, which are to be assessed on a case-by-case basis, for example related to fire damage.
5. Most requests for Finance Committee contingencies relate to unforeseen events or opportunities arising in the normal course of business during the year; where the new activity generates significant additional cost e.g. legal costs of an appeal; or a change in planned approach to IT, requiring work in year. The Committee has raised concerns that departments and service committees are turning too quickly to requesting additional funding, rather than prioritising current spend. Additionally, departments tend to underspend at year end (the 2017/18 outturn position was an underspend on local risk of £12.4m across the three funds) and so arguably did not need the additional resource allocation. The proposed approach will limit

underspends being created where allocated resources can cover the unforeseen costs.

6. However, without provision for clearly exceptional items, Members may feel that waiting towards the year end for funding allocation is not responsive enough. For example, an exceptional unexpected event such as the fire at Epping Forest; or where a budget head doesn't exist. Requests may also be made where the timing of normal business activities changes, for example, funding for the due diligence for a site in relation to the Markets Consolidation Programme. For timing differences, the allocation is expected to be reimbursed later in the year, or future year's spend reduced. As it is difficult to devise 'hard and fast' rules as to what constitutes 'exceptional', it is recommended that such items are identified on a case by case basis.
7. Where contingency funding is not granted and a department overspends, the Finance Committee may waive the usual arrangements for clawing back the deficit from the following year's budget allocation.

Are contingencies of an adequate level?

8. Both Policy and Resources and Finance Committees receive monthly reports setting out contingency fund allocation and future commitments against these funds to ensure transparency and clarity on where funds have been allocated and the remaining funds available.
9. Over recent years, the contingencies have proved to be adequate and spend has been well within resource, particularly for the Finance Committee contingency.
10. In addition to these contingency funds, the City Corporation maintains a strong reserve position as mitigation for the general risks that come with the City Corporation's operations and the complex environment it operates in. If a substantial issue emerged which was beyond the capacity of the contingency funds, the City Corporation would be able to utilise its reserve balances to support the City Corporation's activities. Any allocation of reserve funding would be subject to approval through the relevant spending committee, Resource Allocation Sub Committee; and Court of Common Council.

Central risk budgets

11. At the September Committee a query was raised regarding the flexibility of central risk budgets to respond to unforeseen events. Whilst most central risk budgets are focused on specific areas of spend, these budgets also include Policy and Resources and Finance Committee contingency funds. Should unforeseen costs occur for central risk items that can't be managed within the overall central risk budget envelope, it is expected that a request would be made to these contingency funds to address the issue.
12. Central risk budgets cover areas of income and expenditure which are subject to fluctuations in actual value that are outside the control of Chief Officers; or where

it is more beneficial to control such income and expenditure streams corporately. Examples of such areas include:

- Strategically important income streams such as investment income;
- Corporate budgets such as capital financing and central contingencies;
- Cost items that are more effectively controlled centrally, e.g. where it would not be appropriate for a Chief Officer to benefit from underspends nor be penalised for overspends;
- Service charge income relating to the recovery of central charges for support costs and insurance; and
- Expenditure items the Chamberlain has agreed to fund centrally, e.g. redundancy costs.

13. This categorisation of budgets was established to enhance accountability and scrutiny of Chief Officers financial management by defining those areas of spend that they can directly manage and control (i.e. local risk budgets) and those which they cannot (central risk budgets). From time to time service committees have requested that certain volatile budget items be moved to central risk, the most recent example of this relates to homelessness.

14. Central risk budgets span across all three funds as well as Guildhall Administration and are subject to the same financial controls and monitoring arrangements as local risk budgets although they are not subject to the local risk overspend carry forward provision.

15. The quarterly budget monitoring reports submitted to your Committee show the overall position of the City Corporation across both central and local risk budgets which allows a holistic view to be taken on the impact of budget variations in either area.

Implications

16. Where contingency funding is approved early in the financial year it is possible that the funding pressure does not materialise and could have been contained within the original budget allocation. Allocating contingency funding in this situation would result in an increased underspend position at year end. The proposal to limit the award of contingency funding to the latter part of the financial year mitigates this situation.

Conclusion

17. Finance Committee's practice on how to treat contingency requests has evolved over the last year. This report recommends a formalisation of that practice, so that departments and service committees requesting additional in-year funding are encouraged to manage within local risk budgets in so far as possible. It is proposed that contingency funding will only be allocated towards the end of the financial year when forecast year end positions are more accurate or in exceptional circumstances.

18. Central risk budgets generally cover strategically important income streams, corporate budgets or known volatile spend or income items, whereas contingencies are for unforeseen items of spend. Should unforeseen costs occur for central risk items that can't not be managed within the overall central risk budget envelope, it is expected that a request would be made to these contingency funds to address the issue.

Appendices

- None

Background Papers

- Central Risk Budget Review, Efficiency and Performance Sub Committee, November 2017

Philip Gregory

Deputy Director, Financial Services
Chamberlain's

T: 020 7332 1284

E: Philip.Gregory@cityoflondon.gov.uk