APPENDIX A

Narrative report

1 . INTRODUCTION TO THE STATEMENT OF ACCOUNTS

1.1 The Authority is legally required to produce a statement of accounts detailing the year's financial activities and the overall financial position at the 31 March. This narrative report provides an overview of the accounts, with a focus on financial performance. This includes how the Authority has delivered economy, efficiency and effectiveness in its use of resources over the year

1.2 The Statement of Accounts for the year ending 31 March 2017 are set out in this document and consist of a number of statements. Much of the information in the document is of a technical nature and has been completed to be compliant with the 2016/17 Local Authority Accounting Code of Practice and Service Reporting Code of Practice. The Statement of Accounting Policies explains the policies adopted by the Council to compile these accounts.

1.3 The Comprehensive Income and Expenditure Account summarises the resources that have been generated and consumed in providing services and managing the Council during the last year. In 2016/17 this was a net deficit of £Xmillion. The statement is compiled in accordance with generally accepted accounting practices, rather than the amount to be funded from taxation. Authorities raise taxation to cover expenditure in accordance with regulations; this may be different from the accounting cost. The taxation position is shown in the Movement in Reserves Statement.

1.4 The Movement in Reserves Statement shows the movement in the year on the different reserves held by the Authority, analysed into 'usable reserves' and other 'unusable' reserves. The starting point for the movement is the Surplus or (Deficit) on the Provision of Services line from the Comprehensive Income and Expenditure Account. There are then a series of statutory adjustments that are required before you get to the amount that is charged to the General Fund Balance for council tax setting purposes. The Net Increase/Decrease before Transfers to Earmarked Reserves line shows the statutory General Fund Balance before any discretionary transfers to or from earmarked reserves undertaken by the Council. The General Fund Balance at the start of the year was £7.1million. This statutory General Fund Balance at the end of the year (before any transfers to earmarked reserves) is £8.2million. It was expected that the General Fund balance would reduce over the year to support service delivery whilst savings were identified. However underspends during the year and increased Business Rates income have resulted in the increase in the General Fund Balance.

1.5 In future years it is still expected that General Fund Reserves will need to be used to support service delivery whilst ways to reduce expenditure or increase income are identified. Reserve levels have been purposely built up in recent years to support this. The current estimate of the minimum level of General Fund reserves is £1.6m.

1.6 Usable reserves are those reserves that the Authority may use to provide services, subject to the need to maintain a prudent level of reserves and any statutory limitations on their use (for example the Capital Receipts Reserve, that may only be used to fund capital expenditure or repay debt). The second category of reserves is those that the Authority is not able to use to provide services. This includes reserves that hold unrealised gains and losses (for example the Revaluation Reserve), where amounts would only become available to provide services if the assets are sold; and reserves that hold timing differences shown in the Movement in Reserves Statement line 'Adjustments between accounting basis and funding basis under regulations'.

1.7 The Balance Sheet shows the value as at the 31 March of the assets and liabilities recognised by the Authority. The net assets of the Authority (assets less liabilities) are matched by the reserves held by the Authority. The value of net assets of the Authority at 31 March 2017 are £Xmillion.

1.8 The Cash Flow Statement shows the changes in cash and cash equivalents of the Authority during the year. The statement shows how the Authority generates and uses cash and cash equivalents by classifying cash flows as operating, investing and financing activities. The amount of net cash flows arising from operating activities is a key indicator of the extent to which the operations of the Authority are funded by way of taxation and grant income or from the recipients of services provided by the Authority. Investing activities represent the extent to which cash outflows have been made for resources which are intended to contribute to the Authority's future service delivery. Cash flows arising from financing activities are useful in predicting claims on future cash flows by providers of capital (i.e. borrowing) to the Authority.

1.9 The Notes relating to the statements are detailed after the statements and provide further detail to the numbers contained within the statements.

1.10 The Authority is a billing authority for the collection of Council Tax and National Non-Domestic Rates (NNDR) for the District. The Collection Fund Account is a notional account to show all the income collected and how it is distributed. Because the Authority is acting as an agent, only the Authority's share of the Collection Fund balance is reflected in the rest of the Authority's accounts and the other statements.

2. MEDIUM TERM PLANNING AND OVERALL FUNDING

2.1 The Authority has a cyclical process to determine its priorities and align both resources and finances to achieve those priorities. The high level priorities for 2016/17 were as follows:

- To work with our partners to provide an attractive and safe environment for our residents, where diversity is welcomed and the disadvantaged are supported
- To promote sustainable growth within our district to ensure economic and social opportunities exist for our communities, whilst remaining mindful of our cultural and physical heritage
- To ensure that the Council delivers cost effective and necessary services to our residents that are responsive to developing need and financial constraints

2.2 The funding announcement from Central Government in December 2016 was that the New Homes Bonus funding would reduce by much more than expected. A reduction in the time period it is paid for and a baseline level have been introduced. This means that the Bonus will only be received for 5 years in 2017/18 (4 years from 2018/19), and will only be paid on housing growth that is more than 0.4% of the current base level. This was in addition to the reductions in Revenue Support Grant announced in December 2015.

2.4 As a result of these funding reductions the Authority anticipates that it will need to deliver around £3.4million of budget reductions over the next 4 years. £3.4m is around 20% of current net expenditure. As part of the MTFS process for 2017/18 onwards, £0.9million of budget reductions have been identified to be delivered during the year.

2.5 The Authority achieved budget reductions of £0.40million in 2016/17 (an over achievement of the budgeted level of £0.36million).

2.6 The net worth of the Authority is £77.7million. This represents the theoretical net value of all the Authority's assets and liabilities. Of this value £59.6million is contained within un-usable reserves. For example, a significant proportion of the Authority's value is contained within its property portfolio. The Authority does, however, have a total of £18.1million (£12.8million at 31 March 2016) of usable reserves at 31 March 2017, which can be used to fund revenue and capital expenditure. The Authority seeks to manage the amount of available reserves in a prudent way to ensure there are adequate resources for unknown financial risks and plans for ongoing capital investment. Even though the Authority has used £Xmillion of its general fund reserves during 2016/17, the remaining balance (£Xmillion) is still significantly above the recommended minimum balance. This minimum balance of £1.7million for 2016/17 was approved by Members of the Council in February 2016. The remainder of the increase in usable reserves is primarily due to funding received from the sale of surplus assets that can be used for future capital investment.

2.7 The Authority participates in the Local Government Pension Scheme. The scheme is administered by Hertfordshire County Council. The net position of the pension fund has a significant impact on the Authority's accounts because of the estimated size of future liabilities. The Authority has been notified by the fund actuary that the net liability has decreased by £7.8million during 2016/17 to £47.8million. This improved position is mainly due to improvements in market conditions and the impact on financial assumptions. The net liability had also decreased during 2015/16 by £7.8million. To add a sentence on capitalised lump-sum if approved.

3. INCOME AND EXPENDITURE

3.1 There was a net deficit on the provision of services of £2.1million in 2016/17 (£2.1million in 2015/16). While this is an accounting reflection of the financial performance of the Authority there are £2.8million of "book entries" included in order to be compliant with the Code of Practice that are not costs to be met by the General Fund or funded by Council tax. In particular, the capital charges for depreciation and impairment of assets and the impact of future retirement benefits. These adjustments are listed in note 7 to the accounts. Once these are removed, there is a net surplus that increases the General Fund by £1.1million. The remaining increase in the general fund balance is a transfer from earmarked reserves of £0.3million.

3.2 The Authority provides regular reports to its Cabinet on forecasts of revenue spend. This is to allow the Cabinet to undertake its role in monitoring the Authority's income and expenditure. The end of year report was presented to Cabinet on 13 June 2017. When expenditure forecasts are presented to Cabinet they reflect the way that the Authority has structured itself i.e. Chief Executive; Customer Services; Finance, Policy and Governance; and Planning, Housing and Enterprise. Further details of what makes up these areas can be found on the Authority's website http://www.north-herts.gov.uk/home/council-and-democracy/council-departments.

3.3 The end of year revenue monitor report also includes:

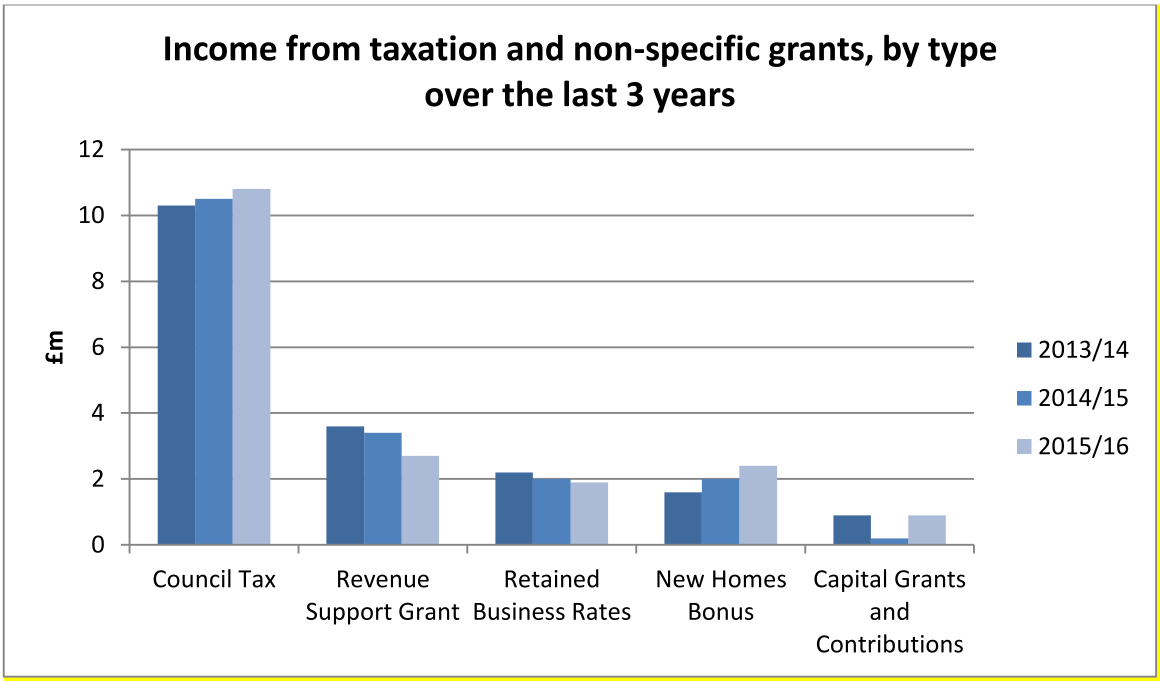
- Explanations for variances from the working budget (latest planned spend), including the impact on future year budgets. Whilst there were a number of variances, there were not any individual significant ongoing impacts reported.
- The level of reserves and balances.

3.4 The Council's Key corporate financial health indicators are monitored throughout the year. These are areas that could have a significant impact on the Authority's budget, and are generally subject to external influences. Of the 4 measures, all performed better than budgeted.

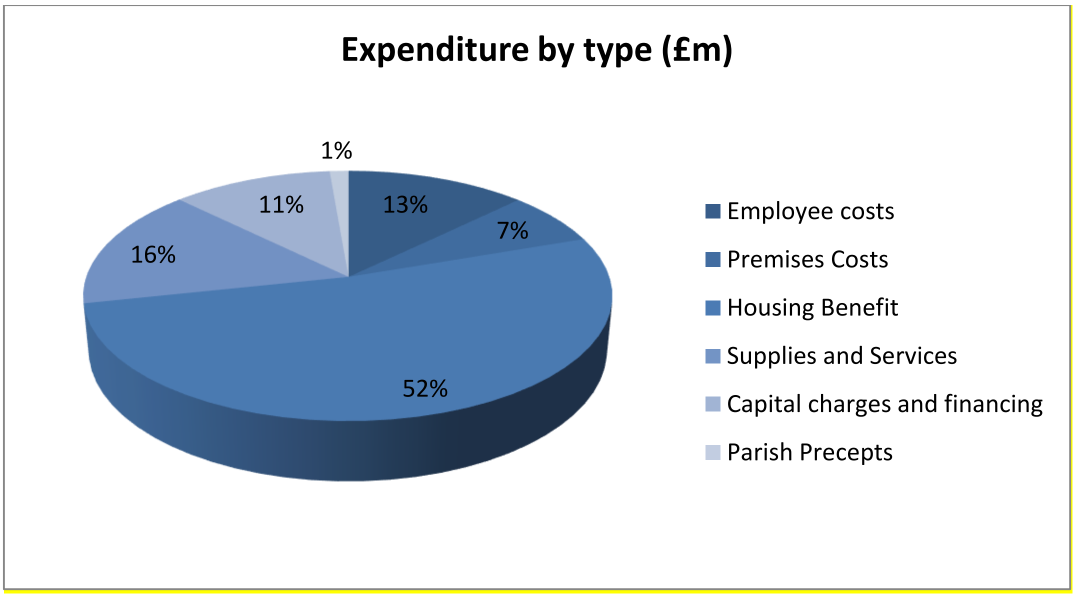
3.5 Although not reported in either the revenue monitor report or the Statement of Accounts, it can be helpful to think about income in terms of where its source and expenditure in terms of what it has been spent on. The next two paragraphs provide this analysis.

3.6 The Authority receives three main types of income:

- Service specific income, which includes specific Government grants and the fees and charges paid by those who use Council services. There is also some income received that relates to contributions and reimbursements. The main specific grant is for Housing Benefit subsidy, which was £38.3million in 2016/17 (£38.3million in 2015/16). The income from fees and charges was £8.2million (£8.2million in 2015/16). On the Comprehensive Income and Expenditure Statement these income sources are shown against the services that they relate to. Overall they total £49.6million, which is 71% of total income.
- Amounts received from investing cash balances and rent received from renting out investment properties. These were £0.5million and £1.0million respectively (the same amount as in 2014/15). This is 2% of total income.
- Income from taxation and non-specific grants. This includes Council Tax, the retained share of Business Rates (NNDR), Revenue Support Grant, New Homes Bonus and Capital Grants. These are detailed in note 10, and total £18.8million (27% of total income). As shown in the chart below, over recent years the balance of funding has started to shift from central grant funding to Council Tax. The Revenue Support Grant funding will disappear from 2017/18. The Authority has seen an increase in the amount of New Homes Bonus funding awarded over the last few years, although changes to the way it is awarded means that it is expected to reduce in future years.



3.6 The 2016/17 gross expenditure for the Authority was £72.8million (£72.8m in 2015/16). This reflects all the Authority's expenditure in the 'Surplus or Deficit on Provision of Services' line in the Comprehensive Income and Expenditure Statement. The largest single item of expenditure was housing benefit payments of £37.8 million, which account for 52% of all expenditure. Capital financing charges account for 11% of the total and consist mainly of payments of interest on loans and contributions for capital expenditure. Employee costs (including associated costs such as training and recruitment costs) account for 13% of costs. Supplies and services, such as operating vehicles and purchase of goods and services represent 16% of the total expenditure. Premises costs (including rents, rates, utilities and repairs and maintenance) made up 7% of costs and the Parish Precept payments to the Parish and Town Councils in the District accounted for 1%.



5. CAPITAL AND BORROWING

5.1 The capital budget for 2016/17 agreed in February 2016 was £8.6million, with a further £11.1million in future years (2017/18 to 2019/20). This budget was increased to £21.1million during the first quarter to reflect 2015/16 projects that had not been completed by the end of that year and additional funding approved by Full Council. The actual spend on capital schemes during the year was £3.5million, of which £1.4million was not funded in the accounts but paid for by drawing down cash investments and increasing the capital financing requirement. The remaining £2.1million was funded from capital receipts, government grants and third party contributions.

5.2 During 2016/17 there has been significant work on the North Herts Leisure Centre in Letchworth. The works commenced in May 2016 and are due to be completed by the end of Summer 2017. The works include a new teaching pool, a new cafeteria, a multi-functional room and refurbishment of the sports hall, changing areas and car park. The value of the works completed in 2016/17 were £Xmillion, of a total forecast cost of £Xmillion. The development will create additional facilities and capacity that will generate additional income (from the contractor) of £216k per year.

5.3 A contract for works on the District Council Offices was signed in February 2017. This will ensure that the building is compliant with current regulations, replaces the ageing façade to make it weather tight, reduces the running costs of the building and improve the use of space to allow co-location with other organisations. The majority of the works will take place during 2017/18, and therefore most of the costs will be incurred during next year.

5.4 There were significant asset disposals during 2015/16 of £5.5million. There have not been any asset disposals during 2016/17, and therefore the capital receipts reserve balance has reduced from £5.5million down to £Xmillion. The Authority still has surplus assets that it will dispose of over time, which will provide further contributions towards capital investment. There can be a significant amount of time between identifying a disposal and actually receiving the money, as most sales are contingent on the purchaser obtaining planning permission. The Authority is looking at ways it can generate the receipts more quickly by obtaining outline planning permission in advance of the sale.

5.5 The Authority continues to be in the position of a negative capital financing requirement (CFR). This means the Authority does not have a debt liability and has not needed to make a minimum revenue provision towards the cost of capital in 2015/16. As at the end of 2016/17 the CFR value was negative £18.7million. This means that the Authority could invest this amount in capital projects without needing to make a Minimum Revenue Provision (MRP). MRP is a charge to the General Fund (and therefore Council Tax) so when required it increases the cost of capital investment. Whilst there is not a need for a MRP, the only revenue cost of capital spend is the lost income on investment balances. Interest on cash investments is at an historic low. As a result, the Authority will continue to invest to capital schemes, but will focus on those schemes that generate income or reduce ongoing running costs. This will therefore help to balance the revenue budget as funding levels reduce.

5.6 In previous years the Authority has funded part of the capital programme from loans. The value of long term loans owed to external parties for capital spending amount to £0.5million as at 31 March 2017. The redemption fees for paying off these loans early means that it is not worth doing so, even though the Authority has the cash investments (£38.0million at 31 March 2017) to be able to do so. The remaining loans will be repaid in small amounts over the next 25 years. This borrowing should be viewed in relation to the value of the assets, which are valued by a combination of replacement cost and historic cost, and have a net book value of £88.1million.

5.7 For 2017/18 - 2020/21 the Authority has an approved capital programme of £16.1million. This was approved by Council on 9 February 2017 and further details can be found on the Authority's website, including the full list of projects and amount of investment. This was budgeted to be funded by:

£000	**2017/18**	**2018/19**	**2019/20**	**2020/21**	**Total**
Capital Receipts	1,291	2,521	1,089	122	**5,023**
Government Grants and Other Contributions	1,901	654	654	941	**4,150**
Revenue Contributions	0	0	0	0	**0**
Unfunded- drawdown on investments (CFR impact)	5,273	1,363	0	331	**6,967**
Total	**8,465**	**4,538**	**1,743**	**1,394**	**16,140**

The use of capital receipts funding assumes that around £5.7million of additional receipts would be generated from the sale of surplus assets during 2017/18 and 2020/21.

5.8 The actual spend in 2017/18 will now be around £20.6million, which reflects that a number of schemes were not completed during 2016/17 and therefore have been reprogrammed in to 2017/18. This is also reflected in the capital receipts balance and negative CFR value being higher than what was budgeted. The Authority will still try and secure grant funding and other contributions, before making use of other funding sources.

6. PERFORMANCE

6.1 A performance report is presented to Overview and Scrutiny Committee on a quarterly basis, with an end of year report presented in June. The year end report for 2016/17 will be presented to the Committee on 6 June 2017 and will be available on the Authority's website. The end of year report highlights performance for the 27 performance indicators. For each indicator the current performance is shown, alongside previous performance, direction of travel and target level (where applicable).

6.2 As at the end of the third quarter, there were five indicators classified as amber. This is where performance is below the target level but is still within agreed tolerances. These related to:

- Percentage of invoices paid on time, 99.49% against a target of 99.6%
- Percentage of NNDR collected in year, 82.3% against a target of 83.8%
- Working days lost due to short-term sickness absence per FTE employee, 2.75 days against a target of 2.4
- Percentage of Housing & Public Protection Service programmed inspections completed, 91.9% against a target of 95%

- Percentage of household waste sent for reuse, recycling and composting, 60.45% against a target of 61%

6.3 The drop in performance of invoices paid on time is mainly due to staff not approving invoices for payment on time, especially around times when they are not in the office. A reminder has been sent to all staff to remind them of the importance of doing this, and also to arrange cover when they know that they will be away. The new version of our accounting system will be implemented during 2017/18 and this will enable the approval workflow to be managed electronically.

6.4 Working days lost due to short-term sickness absence per FTE employee are above target, and higher than they have been in recent years. The HR team are investigating any possible causes or patterns. The target level set is a challenging target, and equates to high performance when compared with other Authorities.

6.5 For the other indicators, it is expected that performance will improve during the remainder of the year and the target may therefore be met. The NNDR collection rates tend to fluctuate during the year and were back on target in January. The Housing and Public Protection Team are recovering from a backlog at the start of the year due to a member of staff leaving. They expect to meet the target level by the end of the year. The household waste data did not include the compostable element of street sweepings as it was not available. This will improve performance.

7. ECONOMIC CLIMATE AND FUTURE PLANNING

7.1 The Authority continues to plan its budget over a number of years by setting a medium term financial strategy (MTFS). The overall strategy was developed at the start of the period of national economic austerity and uncertainty, which has played a significant part in generating the financial pressures the Authority has experienced. This is because the Central Government is seeking to reduce the financial support that it provides to Local Authorities. There is also significant demographic pressure on Social Care authorities, which means that Central Government is looking to transfer funding away from lower tier Authorities, like North Hertfordshire. The Authority plans for the future based on the best available information on future funding, but are also mindful that there could be further reductions in funding up to 2019/20. For example, there could be further changes to the baseline for New Homes Bonus. It is also expected that austerity will continue beyond the current parliament and therefore the Authority should expect further reductions in funding alongside the introduction of 100% business rate retention.

7.2 The impact of the United Kingdom leaving the European Union (EU) is still highly uncertain, which means that the Authority does not consider it worthwhile to undertake detailed planning. The Authority does not have (or forecast to have) any significant income either directly or indirectly from EU funding sources, such as EU grants or Local Enterprise Partnership (LEP) funding.

7.3 Whilst the Authority is currently planning to use significant General Fund reserves over the next few years, the forecast balance at the end of £3.2million at the end of 2020/21 is still above the expected minimum balance of around £1.6million. This therefore gives the

Authority some further protection to deal with any future funding changes or spending pressures. The decision by Council to increase Council Tax by £5 reflects the pressures that the Authority is facing and therefore the need to maximise income.

7.4 The Authority is looking at ways that it can operate more commercially to provide income to support its General Fund activity. This includes making use of the general power of competence that was introduced in the Localism Act of 2011. The Authority is progressing towards setting up a property company that would enable it to generate income from letting market housing. Alongside an existing property, there is £3million allocated in the capital programme for purchasing or building property. The Authority will consider the economic climate before investing in the company. It is likely that demand for housing in the District will remain very high and there will continue to be a need for rental properties, and rental yields should reflect this. The investment will target ongoing rental income and therefore will not be susceptible to fluctuations in the capital value of housing.

7.5 The current economic climate means that interest rates continue to be at a historically low level. There are emerging signs that there will be an increase in the Bank of England base rate. Whilst the Authority does have some borrowing this is at historic fixed rates and therefore is not affected by interest rate changes. The Authority currently has significant cash investments, mainly from capital reserves and General Fund balance. Our current forecasts do not assume any increase in the return received on these investments. The most significant reduction in our cash balances will be from capital investment (e.g. works to the District Council Offices). The capital programme is kept under regular review and there are formal review points built in to the MTFS policy. Any future significant capital investment will need to be assessed on the basis that it may need to be funded from borrowing, and therefore any business case will need to reflect the costs of doing this.

7.6 Most of the Authority's commercial assets are ground leases and therefore not susceptible to fluctuations in property values. These leases generally have at least 50 years remaining and therefore provide an ongoing income stream.

8. SERVICE DELIVERY AND EMPLOYEES

8.1 The Authority has a statutory duty to deliver a number of services, as well as currently choosing to deliver some services that it is not required to do so. For some of these services it is able to recover from the recipient some or all of the cost of providing that service. Other services have to be provided free at the point of use, it would be impractical to charge those that used them or a policy decision is made that they will not be charged for.

8.2 Some of the Authority's services are contracted out, such as waste collection and grounds maintenance. Whilst the contractor takes on the day-to-day delivery of the service, there is still a need for the Authority to monitor performance, and act on any under-delivery.

8.3 The Authority has 324 people that are directly employed (as at 31st March 2017). Of this total 9 are in Senior Management Positions. The table below shows a breakdown of these totals by gender.

	All Employees		Senior Management	
	Number	**Full time equivalent**	**Number**	**Full time equivalent**
Male	107	102.26	7	7
Female	217	182.63	2	1.86
Other	0	0	0	0
Total	**324**	**284.89**	**9**	**8.86**

9. INTERESTS IN COMPANIES AND OTHER ENTITIES

9.1 Local Authorities have to consider all their interests, subsidiaries, associates and joint ventures and where material include the value of the interest in Group Accounts.

9.2 The Authority is engaged in a jointly controlled operation for the provision and management of CCTV in the Hertfordshire and Bedfordshire area. This arrangement is with Stevenage Borough Council, North Hertfordshire Council, East Hertfordshire Council and Hertsmere Borough Council. Each member of the arrangement accounts for their share of the assets, liabilities and cash flows of the CCTV in their accounts. In 2013/14 all partner authorities agreed to incorporate a new company to conduct the commercial trading affairs of the CCTV partnership. This new company, Hertfordshire CCTV Partnership Ltd, started trading on the 1 April 2015. The Authority's interest in this company is not considered to be material, and therefore it is not included within the Statement of Accounts.

9.3 The Authority has set up a joint Building Control Company with six other Hertfordshire Authorities. The company began trading in August 2016. The company will deliver statutory building control services on behalf of the Authority, as well being able to access further areas of work to help spread the cost of the service. The Authority's interest in this company is not considered to be material, and therefore it is not included within the Statement of Accounts.

10. POST BALANCE SHEET EVENTS

10.1 Events may occur between the balance sheet date and the date the accounts are signed by the Strategic Director of Finance, Policy and Governance which may have a bearing on the financial results of the year. Under IAS 10 (Events after the reporting period) there is a requirement to disclose the date after which events will not have been recognised in the Statement of Accounts. This date is 30th June 2017; this being the date the un-audited statement of accounts are signed by the Strategic Director.

11. FURTHER INFORMATION

11.1 Where references are made to reports that are presented to Council, Cabinet and Overview and Scrutiny, these reports can be found on the Authority's website. They can be found by selecting the link to 'view meetings, agendas, minutes and reports' on this page http://www.north-herts.gov.uk/home/council-and-democracy/council-and-committee-meetings.

11.2 Further information about the accounts can be obtained by contacting the Strategic Director of Finance, Policy and Governance at Town Lodge, Gernon Road, Letchworth Garden City, Hertfordshire, SG6 3HN.