

REPORT FOR RESOLUTION

REPORT TO: City Council - 4th March 2009
SUBJECT: Legal Background to Setting of Budget and Council Tax
REPORT OF: The Chief Executive and The City Solicitor

Summary

This report aims to assist all members of the Council in consideration of the complex legal background to their budgetary and Council Tax decisions and in particular to set out the legal factors and requirements which Members of the City Council need to consider in reaching decisions on the budget and Council Tax.

The Report is structured as follows:-

Parts 1 - 2 deal with the principles of Council Tax setting and the general legal duties of the City Council in decision-taking.

Parts 3 - 5 deal with calculating the budget requirement and "capping".

Part 6 deals with calculating the City Council element of the Council Tax.

Part 7 deals with setting the overall Council Tax

Part 8 deals with the respective roles of the Executive, the Overview and Scrutiny committee, and the Council.

Part 9 deals with restrictions on voting for members with Council tax arrears.

Recommendations

That the Executive, the Resources and Governance Overview and Scrutiny Committee and the City Council take this advice into account and follow its principles in reaching decisions in relation to the budget and Council Tax for 2009/10.

Wards affected: All

Implications for:

Equal Opportunities
Yes

Risk Management
Yes

Legal Considerations
Yes

Financial Consequences for the Revenue Budget

The calculation of the budget requirement effectively sets the revenue budget for 2009/10.

Financial Consequences for the Capital Budget

Capital expenditure can be financed out of the revenue budget, if Members so determine.

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Background Documents (available for public inspection)

Report to City Treasurer and Executive Member for Finance and Human Resources and Decision of the City Treasurer on the Council Tax Base 2009/10 dated 25th January 2009.

LEGAL BACKGROUND TO REVENUE BUDGET AND COUNCIL TAX

1. INTRODUCTION

- 1.1 The Council Tax is basically a tax on property with a personal element in the form of a discount in respect of dwellings with less than two relevant residents. All dwellings are listed in one of eight valuation bands and the amount of Council Tax payable in respect of each dwelling (before discounts and other reductions) is in a set proportion between each band. The Headline Tax is calculated for Band D and the tax in the remaining bands is worked out as a proportion of this amount. The lowest Band (A) is two-thirds of Band D and the highest Band (H) is twice Band D and three-times Band A. The proportions are as follows:-

A:	B:	C:	D:	E:	F:	G:	H:
6:	7:	8:	9:	11:	13:	15:	18:

- 1.2 There are three main stages in setting the Council Tax:-

STAGE 1 -	The Council calculates its own budget requirement, i.e. its net revenue expenditure - this is the amount which is subject to capping by the Secretary of State.
STAGE 2 -	The Council then calculates the Manchester City Council element of the Council Tax for all bands based on a calculation for Band D - this will take account of the Council Tax base calculated at an earlier stage.
STAGE 3 -	Finally, the Council sets the Council Tax for the area, being the aggregate of the City Council element of the tax and the element of the tax calculated by the Police Authority and the Fire and Civil Defence Authority.

2. THE COUNCIL'S LEGAL DUTIES

- 2.1 In coming to decisions in relation to the revenue budget and the Council Tax the City Council - and Councillors - have various legal duties, namely:-
- The Council must act in accordance with its statutory duties and responsibilities.
 - The Council must act reasonably.

- (c) The Council must not act in breach of its fiduciary duty to its ratepayers and Council Tax payers.

2.2 Reasonableness

The Council must act in accordance with the principles set out in the case of Associated Provincial Picturehouses Limited -V- Wednesbury Corporation, that is, it must take into account relevant considerations, it must not have regard to irrelevant considerations, and it must not reach a decision which is unreasonable in the sense that it is so irrational or perverse that no reasonable authority could have reached it.

2.3 Fiduciary Duty

Fiduciary duty is hard to define. In Roberts -V- Hopwood (1925), it was said that a local authority charged with the administration for definite purposes of funds contributed in whole or in part by ratepayers owes a duty "to conduct that administration in a fairly business-like manner with reasonable care, skill and caution, and with a due and alert regard to the interest of those (ratepayers)" towards whom the authority "stands somewhat in the position of trustees or managers of the property of others". The same principle applies in relation to Council Tax payers.

Fiduciary duty will probably include the following considerations:-

- (a) Prudent use of the Authority's resources, including the raising of income (such as rents and other charges) and the control of expenditure;
- (b) Awareness of the financial consequences of any proposal of Council Tax payers and Ratepayers;
- (c) Financial prudence both in the short and long term;
- (d) Striking a fair balance between the interests of Council Tax payers and ratepayers on the one hand, and the community's interest in adequate and efficient services on the other hand;
- (e) Acting in good faith with a view to complying with statutory duties and exercising its statutory powers for the benefit of the community.

2.4 Statutory Duty

As part of the budget and the Council Tax fixing process, the Council is required by the Local Government Finance Act 1992 to make various specific calculations and decisions:-

- (a) it must calculate its budget requirement in accordance with Section 32 of the Act:

- (b) it must calculate the City Council element of the Council Tax - first for Band D and then for all bands - in accordance with Sections 33 to 36;
- (c) it must set the overall Council Tax for each band in accordance with Section 30.

These requirements will now be analysed in greater detail.

3. **STAGE 1 - THE COUNCIL'S BUDGET REQUIREMENT**

3.1 Section 32 of the LGFA 1992 requires the Council to make three calculations, in effect -

- (i) an estimate of the Council's gross revenue expenditure - Section 32(2);
- (ii) an estimate of anticipated income - Section 32(3)
- (iii) a calculation of the difference between (i) and (ii) above, (i.e. net revenue expenditure) - Section 32(4).

3.2 More specifically, in its Section 32(2) calculation of gross expenditure the Council should include -

- (a) estimated revenue account expenditure to be incurred during the year;
- (b) an appropriate allowance for contingencies (i.e. an allowance for unforeseen events);
- (c) any raising of reserves for future years (e.g. payments into special funds);
- (d) any estimated revenue account deficit for previous years not already provided for;
- (e) an estimate of certain amounts to be transferred to the collection fund pursuant to a direction of the Secretary of State (e.g. any estimated shortfall in collection of National Non-Domestic Rates (NNDR) in excess of allowance for non-collection).

3.3 The Section 32(3) calculation is the aggregate of the sums to be set off against gross expenditure, namely -

- (a) estimated income from fees, charges and most specific grants (but excluding Revenue Support Grant (RSG) redistributed NNDR and additional grant for previous years)
- (b) an estimate of certain transfers from the collection fund to the general fund e.g. allowance for costs of collecting business rates;

- (c) any amount of reserves/balances intended to be used towards meeting revenue expenditure.
- 3.4 Section 32(4) then requires the calculation under Section 32(3) to be subtracted from that under Section 32(2) to produce a calculation of estimated net expenditure known as the budget requirement.
- 3.5 These calculations must be made before 11th March, although they are not invalid merely because they are made on or after that date. However, until the calculations are made any purported setting of the Council Tax will be treated as null and void.
- 3.6 It should be noted that the general fund has to stand the cost of any temporary lending to the collection fund to cover late payments/non-collection.
- 3.7 In making the Section 32 calculations, the Council will need also to calculate the level of financial reserves which it proposes to leave in balances.
- 3.8 Schools budget related expenditure is no longer financed through RSG, NNDR and council tax, but rather through a ring-fenced Dedicated Schools Grant (DSG). Schools expenditure calculated under Section 32 (2)(a) will be offset by the DSG which will be included in the calculation under Section 32 (3)(a), thereby reducing both the amount of the budget requirement and the amount of RSG received.

4. **THE LEVEL OF THE BUDGET REQUIREMENT**

- 4.1 The level of the Section 32 calculations, and in particular the calculation of the budget requirement is of crucial importance both legally and financially. In particular -
- the amount of the budget requirement must be sufficient to meet the Council's budget commitments and thereby ensure a balanced budget.
 - the amount of the budget requirement must leave the Council with adequate financial reserves.
 - the level of the budget requirement must not be unreasonable having regard to the Council's fiduciary duty to its Council Tax payers and ratepayers.
 - the amount of the budget requirement may determine whether or not the Council is designated for "capping".

4.2 **Adequacy of Budget Requirement and Financial Reserves**

As has been seen, Section 32 requires the Council to calculate its gross expenditure under 5 separate headings and its offsetting income under three headings. Beyond that, the Act offers no guidance as to the detail in which the estimates are to be formulated.

- 4.3 However, the Local Government Act 2003 requires the Chief Finance Officer to report to the authority on the robustness of the estimates made for the purposes of the calculations and the adequacy of the proposed financial reserves. This will include estimates and reserves used for the purpose of the Executive's recommendations to Council and for the purpose of any amendments to those recommendations. The Council has a statutory duty to have regard to the Chief Finance Officer's report when making decisions about the Section 32 calculations.
- 4.4 If the calculation of the budget requirement is insufficient to meet budget commitments, there are obvious practical as well as legal consequences for the Council. It is appropriate at this point to mention the duties imposed on the Council and the City Treasurer as Chief Finance Officer of the Authority.
- 4.5 Section 28 of the Local Government Act 2003 imposes a statutory duty on the Council to monitor during the financial year its expenditure and income against the budget calculations. If the monitoring establishes that the budgetary situation has deteriorated, the Council must take such action as it considers necessary to deal with the situation. This might include, for instance, action to reduce spending in the rest of the year, or to increase income, or to finance the shortfall from reserves.
- 4.6 Under Section 114 of the Local Government Finance Act 1988, where it appears to the Chief Finance Officer that the expenditure of the authority incurred (including expenditure it proposes to incur) in a financial year is likely to exceed the resources (including sums borrowed) available to it to meet that expenditure, the Chief Finance Officer has a duty to make a report to the Council.
- 4.7 The report must be sent to the Council's Auditor and every member of the Council and the Council must consider the report within 21 days at a meeting where it must decide whether it agrees or disagrees with the views contained in the report and what action (if any) it proposes to take in consequence of it. In the intervening period between the sending of the report and the meeting which considers it, the authority is prohibited from entering into any new agreement which may involve the incurring of expenditure (at any time) by the authority, except in certain limited circumstances where expenditure can be authorised by the Chief Finance Officer. Failure to take appropriate action in response to such a report may lead to the intervention of the Council's Auditor.

4.8 The Level of Section 32 Calculations

The next issue relates to the reasonableness of the level of expenditure calculated under Section 32. There were a series of cases in early 1980's where Plaintiffs sought to challenge the legality of the rate by arguing that a local authority was in breach of its fiduciary duty and acting unreasonably by overspending. Although such an argument succeeded in the case of R -V- GLC, ex parte, London Borough of Bromley, the Courts restricted the ambit of that decision in subsequent cases. Whilst the Courts have avoided saying

that a high level of expenditure will never be unreasonable, it does now seem that expenditure levels will not be regarded as unreasonable provided that they can be justified, are not irrational and the Authority is taking into account all relevant considerations, including the fiduciary duty to those paying the tax. (R -V- Waltham Forest LBC, ex parte Baxter).

- 4.9 In reaching decisions on expenditure levels Councillors must not fetter their discretion by treating as decisive a proposal or proposals in their election manifesto. Each decision must be reached anew in the light of all known factors, but members may properly take into account their election manifesto when deciding between lawful options.
5. **"CAPPING"**
- 5.1 Part II of the Local Government Act 1999 instituted a new and rather complicated regime in relation to "Capping" of expenditure. Nevertheless, the Secretary of State still retains wide reserve powers where in his/her opinion the amount calculated by an authority as its budget requirement is excessive.
- 5.2 The Secretary of State must first decide if the budget requirement is excessive. S/he will determine a set of principles which will be used to decide this and the principles must include a comparison with the budget requirement of previous years. Manchester's budget requirement in 2008/09 was £457,290,718.
- 5.3 The Minister for Local Government has indicated that he would expect to see Council tax increases to be "substantially below 5%".
- 5.4 If the Secretary of State decides the budget requirement is excessive, s/he may designate the authority "in-year" (i.e. for that financial year), or s/he may exercise a range of alternative powers.
- 5.5 Where an authority is designated for capping "in-year", the legislation provides for the following procedure. The Secretary of State must notify the authority in writing that it has been designated, the principles applied and the amount which s/he proposes should be the maximum amount for the budget requirement. The authority then has 21 days to accept the maximum amount or to challenge it and put forward an alternative which will have to be considered by the Secretary of State. If s/he still considers that the authority should be capped "in-year", s/he may fix an amount which is the same, or greater or smaller than, that stated in the original notice. The authority will then be required to make substituted calculations to comply with the expenditure limitation. If the original council tax demands have already been prepared or sent out, the authority would have to prepare and send out revised demands - thereby delaying the receipt of council tax income and incurring additional interest charges. It would then have to make cuts in expenditure with immediate effect without any "breathing space" to mitigate their impact.

5.6 However, Part II of the 1999 Act gives the Secretary of State alternative powers:

- * S/he may cap an authority for the following year, thereby avoiding the re-billing costs of "in-year" capping.
- * S/he may cap an authority over a number of years, starting either in-year or the following year, and enabling expenditure to be reduced over longer periods.
- * S/he may decide not to designate an authority but to set a notional (lower) budget requirement for the year under consideration which will be taken into account instead of the actual budget requirement for the purpose of any future comparisons with that year's budget.

6. **STAGE 2 - CALCULATING CITY ELEMENT OF COUNCIL TAX**

6.1 Having calculated its budget requirement, the Council is then required to calculate its own element of the Council Tax first for Band D (Section 33) and then for all 8 bands as a proportion of the Band D calculation (Section 36). The City element of the Council Tax has to finance that part of the budget requirement which cannot be financed by RSG and redistributed non-domestic rates, plus the Council's share of the deficit on the collection fund.

6.2 **The Section 33 Calculation**

The City Element of the Band D Council Tax is known as the basic amount of Council Tax. This is calculated by applying the following formula -

$$\frac{R-P}{T}$$

where -

R is the budget requirement

P is the aggregate of RSG redistributed non-domestic rates and additional grant for previous years, reduced by the estimated collection fund deficit (or increased by any estimated surplus)

T is the Council Tax base.

6.3 **Collection Fund Deficit**

Any deficit on the collection fund from preceding years has to be financed through the Council Tax. Such a deficit is shared "pro rata" with the precepting authorities. The required calculations had to be made on 15th January and the appropriate shares of the deficit notified to the precepting authorities.

6.4 Council Tax Base

The Council Tax base is basically the Band D - equivalent number of properties in the City adjusted to take account of discounts etc and multiplied by the estimated collection rate. The City Treasurer acting under delegated powers has calculated the council tax base for 2009/10 to be 121,127 an increase from 118,844 in 2008/09.

6.5 The Section 36 Calculation

Having calculated the basic amount of Council Tax (i.e. the City element of the Band D tax) the Council is then required to convert it into a City element for all Bands by multiplying it by the formula N/D where -

N is the proportion for the band as set out below and D is 9.

6.6 The proportions for each band are as follows:-

A:	B:	C:	D:	E:	F:	G	H:
6:	7:	8:	9:	11:	13:	15:	18

6.7 The Council's demand on the Collection Fund

One further calculation to be made is of the amount to be transferred from the collection Fund to the General Fund during the year, i.e, the Council's demand on the Collection Fund. In effect, this amount will be that part of the budget requirement not financed by RSG and redistributed NDR, plus the Council's share of the Collection Fund deficit. Another way of putting this is the formula set out in Section 97(1) of the Local Government Finance Act 1988, namely -

$$B \times T$$

Where -

B is the basic amount of Council Tax calculated under Section 33 (i.e the City element of Band D, and
T is the Council Tax base.

7. STAGE 3 - SETTING THE COUNCIL TAX

7.1 The final part of the process is for the Council as billing authority to set the overall Council Tax for each band. Whereas the billing authorities and major precepting authorities calculate their own budget requirements, their own basic amounts and amounts for each band, the setting of the Council Tax is solely the responsibility of the City Council as billing authority.

7.2 Section 30 of the 1992 Act provides that the amounts set for each band will be the aggregate of the City element for each band calculated under Section 36 and the amount calculated for each band by each of the major precepting authorities.

- 7.3 The Council Tax must be set before 11th March (i.e no later than 10th March), although it is not invalid merely because it is set on or after that date.
- 7.4 The Council Tax cannot be set before 1st March unless all precepting authorities have issued their precepts; nor can it be set before the Council has made the other required calculations. Otherwise, any purported setting of the tax will be treated as not having occurred.
- 7.5 The City Council has a clear legal duty to set a Council Tax and a resolution not to set a Council Tax would be unlawful, being in breach of Section 30, LGFA 1992. So would be a resolution to set a Council Tax which deliberately did not balance the various calculations.
- 7.6 A draft resolution for setting the Council Tax is attached at Appendix 1.

8. **CONSTITUTIONAL ARRANGEMENTS**

- 8.1 Members should note that under the Council's constitutional arrangements, the functions of calculating the budget requirement and the City element of the Council Tax and the function of setting the Council tax are the responsibility of the full Council. The function of preparing estimates and calculations for submission to Council is the responsibility of the Executive.
- 8.2 The Council's Constitution provides a procedure for the resolution of any conflict between the Executive and the Council which gives effect to the Local Authorities (Standing Orders) (England) Regulations 2001. However, this only applies where the estimates and calculations are prepared by the Executive before 8th February. That will not happen this year and any conflict can be resolved through the scrutiny process. The Budget and Policy Framework Rules provide that where the Resources and Governance Overview and Scrutiny Committee has any objection to the estimates and calculations prepared by the Executive, it will report such objections to the Council, the Leader and the Executive Member for Finance and Human Resources. The Leader and/or the Executive Member will report to the Council whether they agree or disagree with any objection of the Overview and Scrutiny Committee.

9. **RESTRICTIONS ON VOTING**

- 9.1 Members should be aware of the provisions of Section 106 of the Local Government Finance Act 1992, which applies to members where -
- (a) they are present at a meeting of the Council, the Executive or a Committee and at the time of the meeting an amount of council tax is payable by them and has remained unpaid for at least two months, and
 - (b) any budget or council tax calculation, or recommendation or decision which might affect the making of any such calculation, is the subject of consideration at the meeting.

- 9.2 In these circumstances, any such members shall at the meeting and as soon practicable after its commencement disclose the fact that Section 106 applies to them and shall not vote on any question concerning the matter in 9.1 (b) above. It should be noted that such members are not debarred from speaking on these matters.
- 9.3 Failure to comply with these requirements constitutes a criminal offence, unless any such members can prove they did not know that Section 106 applied to them at the time of the meeting or that the matter in question was the subject of consideration at the meeting.

10. **RECOMMENDATIONS**

The Executive, the Resources and Governance Overview and Scrutiny Committee and the City Council are asked to take this advice into account and to follow its principles in reaching decisions in relation to the budget and Council Tax for 2009/10.

APPENDIX 1

COUNCIL TAX DRAFT RESOLUTION SETTING THE AMOUNT OF COUNCIL TAX FOR THE COUNCIL'S AREA

RESOLVED

1. That the estimates prepared by the Executive at its meeting on 11th February 2009 be [approved/amended as follows]
2. That it be noted that the City Treasurer acting under delegated powers has determined the amount of [121,127] as the Council Tax base for Manchester for the year [2009/10] in accordance with Section 33(5) of the Local Government Finance Act 1992 and regulations 3 and 5 of the Local Authorities (Calculation of Council Tax Base) Regulations 1992, as amended.
3. That the following amounts be now calculated by the Council for the year [2009/10] in accordance with Sections 32 to 36 of the Local Government Finance Act 1992:-
 - (a) £ being the aggregate of the amounts which the Council estimates for the items set out in the Section 32(2)(a) to (e) of the Act.
 - (b) £ being the aggregate of the amounts which the Council estimates for the items set out in Section 32(3)(a) to (c) of the Act.
 - (c) £ being the amount by which the aggregate at 3(a) above exceeds the aggregate at 3(b) above, calculated by the Council, in accordance with Sections 32(4) of the Act, as its budget requirement for the year.
 - (d) £ being the aggregate of the sums which the Council estimates will be payable for the year into its general fund in respect of redistributed non-domestic rates, revenue support grant or additional grant reduced by the amount of the sums which the Council estimates will be transferred in the year from its general fund to its collection fund in accordance with the formula set out in Section 33(3) of the Local Government Act 1992, as amended.
 - (e) £ being the amount at 3(c) above less the amount at 3(d) above, all divided by the amount at 2 above, calculated by the Council in accordance with Section 33(1) of the Act, as the basic amount of its Council tax for the year.

(f)

Valuation Bands

A B C D E F G H

£

being the amount given multiplying the amount at 3(e) above by the number which, in the proportion set out in Section 5(1) of the Act, is applicable to dwellings listed in a particular valuation band divided by the number which in that proportion is applicable to dwellings listed in valuation band D, calculated by the Council, in accordance with Section 36(1) of the Act, as the amounts to be taken into account for the year in respect of categories of dwellings listed in different valuation bands.

4. That it be noted that the following amount to be transferred by the Council for year [2009/10] from its collection fund to its general fund in accordance with Section 97(1) of the Local Government Finance Act 1988:-

£ being the amount given by multiplying the amount at 3(e) above by the amount at 2 above.

5. That it be noted that for the year [2009/10] the major precepting authorities have stated the following amounts in precepts issued to the Council, in accordance with Section 40 of the Local Government Finance Act 1992, for each of the categories of dwellings shown below:-

Precepting authority Valuation bands

A B C D E F G H

GM Police Authority £

GM Fire and Civil
Defence Authority £

6. That, having calculated the aggregate in each case of the amounts at 3(f) and 5 above, the Council, in accordance with Section 30(2) of the Local Government Finance Act 1992 hereby sets the following amounts as the amounts of Council Tax for the year [2008/09] for each of the categories of dwellings shown below.

Valuation bands

A: B: C: D: E: F: G: H: