FINANCE REPORT

Purpose

1. To provide the National Committee with an update on:

- Forestry Commission England and Central Services (FCE/CS) financial position at end August (Period 07);
- Business Planning; and,
- the finance risk assessment.

2016/17 Financial Position – End October (Period 07)

2. The summary forecast position of the various FCE/CS budget targets is illustrated in the following table:

	Original Budget £m	ExCo Approved Budget £m	Period 07 Forecast £m	Indicative Variance/ Pressure £m
Net RDEL	44.2	44.2	44.4	0.2
Net CDEL	4.7	7.2	7.6	0.4
Net RAME	-0.4	-0.4	-0.4	0.0

3. The Approved Budget reflects approval by the Defra Executive Committee (ExCo) of the following budget variances:

- RDEL - the £877k balance of the £1m Forestry Innovation Fund (FIF);
- RDEL - (£935k) depreciation reduction;
- RDEL - £100k Deer Initiative Funding switch from Natural England;
- RDEL – (£100k) pro-rata corporate services reduction share;
- CDEL - £1.6m Woodland Carbon Fund (WCF);
- CDEL - £930k capital for Forest Research estates renovation work, notably replacement windows at Alice Holt.

4. The FIF, WCF and FR estates values will be regularised through the Supplementary Estimates budget switching exercise, the other values managed through the Risk & Opportunities tracker.

5. The forecast also includes the following items which have received indicative approval by Defra officials in anticipation of ExCo endorsement:

RDEL

- £150k RDPE Technical Assistance (TA) funding;

CDEL

- £100k to enhance a felling database to support the boundary alignment work with EA/NE;
- £76k FR Capital Science Equipment, and,
- £60k to allow FR to take forward further renovation work on their estate.

6. The following matters remain pending on our Risks & Opportunities tracker, namely:

RDEL

- £40k estimated cost for administering the Woodland Carbon Fund (WCF).

CDEL

- £180k for IS 'run & maintain items'. An annual issue linked to the legacy of not having a capital baseline through SR10.This value is included in the forecast.

7. The following table reconciles the forecast to the Approved Budget:

	£m
RDEL Approved Budget	**44.2**
Add RDPE Technical Assistance	0.15
Add WCF administration costs	0.04
RDEL Forecast	**44.4**
CDEL Approved Budget	**7.20**
Add Felling Database	0.10
Add FR Science Equipment	0.08
Add FR Estates	0.06
Add IS 'Run & Maintain'	0.18
CDEL Forecast	**7.62**

8. The FC Tax Programme continues to progress well with a field trip by HMRC to North England Forest District in late September. The current best estimate of liabilities for FEE, established on the advice received from external advisors, is £3.2m based on a 2015/16 liability of £800k over a four year period, plus interest and penalties. This figure is recorded in our Risks & Opportunities Tracker, but not in the above forecast.

9. Senior Defra officials have been alerted to the issue and the risk of liabilities being required to be paid to HMRC in 2016/17, which if not funded would inevitably have a severe adverse impact on FEE's reserves and ongoing capital programme. We will hold further discussions with Defra Finance colleagues as the liability position becomes clearer through ongoing dialogue with HMRC.

10. The RDPE forecast continues to anticipate spending the gross budget of £26.0m in full.

11. Annex A sets out the forecast financial position in more detail. The apparent overspend on FR Programme RDEL is a temporary issue caused by a delay in finalising the value of research and development costs which need to be capitalised into CDEL. This is also why the CDEL actuals figure is low.

12. Annex B provides further background on FEE's financial position.

Business Planning

13. Our internal business planning work for 2017/18 continues at pace with primary business areas submitting their plans for Director England and Finance Director scrutiny in November, with the overall plan to be finalised early in the New Year prior to seeking ENC approval.

14. In parallel we are actively engaged at a senior level in Defra's business planning prior to the Big Room Event on 28th November.

15. Defra have adopted a new method of resource allocation for 2017/18 and beyond which is based on their new Target Operating Model (TOM). The Group need to save approximately £300m annually by the end of 2019/20. This is broadly split as follows:

- £164 million from corporate services transformation;
- £80 million from transformation in other parts of the business; and,
- £50 million from policy choices agreed in SR15.

16. Of the £80 million transformation savings, £8 million has already been made through policy and evidence reductions in core Defra. This leaves £72 million from transformation in other parts of the business. ExCo have decided that £32m will be delivered through the six vertical outcome systems and £40m through the cross-cutting horizontal programmes.

17. It is clear that FC will be required to play a part in delivering these savings which are front-loaded in the early part of SR15, and may be exacerbated with announcements from the Chancellor in his Autumn Statement on 23rd November. This will be difficult given the significant level of savings already built into our 2016/17 baseline, including highly optimistic policy choice reductions, the anticipated increased recurrent tax bill due to a changed basis for tax recovery, the requirement to administer the WCF, and the costs of non-legislative forestry reform. Some difficult decisions therefore seem inevitable.

Finance Risk Assessment

2016/17 Budget

18. Although a balanced budget is in place for FCE/CS, there is a risk that Defra's already finely balanced forecast position will deteriorate; pressure for further contributions to group savings cannot be ruled out and would compound the potential tax-related pressures.

HMRC Compliance Audits

19. The financial and reputational risk posed by the current HMRC compliance audits into PAYE and VAT has been fully recognised, and steps taken to deal quickly with issues as they arise and to ensure that our guidance and procedures are made fully compliant as soon as possible.

20. However, and as mentioned above, the potential liabilities arising from the audit could be significant and would place additional stress and strain on our finances, particularly FEE.

2017/18 Business Plan

21. There is a significant risk that FCE/CS will be required to make further significant reductions in order to assist Defra in meeting its challenging savings targets.

Recommendations

22. The Committee is invited to note and discuss:

- the financial position as at end October (AP07);
- the update on Business Planning; and,
- the finance risk assessment.

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November 2016