APPENDIX D

LOCAL GOVERNMENT ACT 2003 – REPORT BY THE CHIEF FINANCIAL OFFICER ON THE ADEQUACY OF RESERVES AND ROBUSTNESS OF BUDGET ESTIMATES

1. INTRODUCTION

1.1 Section 25 of the Local Government Act 2003 requires the Chief Finance Officer and Section 151 Officer to formally report to Council as part of the tax setting report on the robustness of estimates and the adequacy of reserves. The Council is required to take this report into account when setting the Budget and Council Tax at its meeting on 24 February 2021.

1.2 In the context of its service and financial planning the Council's overall approach to risk management is to take appropriate action to mitigate risks, or ensure that sufficient contingency exists, so that service provision is not threatened by unforeseen financial problems during the financial year.

1.3 Making changes to service provision at short notice in order to resolve a budget problem can have undesirable consequences. These can include:

(a) damage to the Council's reputation and customer relationships if services are unavailable or delayed

(b) failure to meet agreed performance targets

(c) inefficiencies in overall service provision

(d) associated costs of reducing service provision, such as staff redundancies, when planning changes over a longer timescale would allow greater flexibility

(e) potential problems for partner organisations that are dependent upon Council financial support to achieve agreed goals.

1.4 To avoid such problems the Council manages its financial risks by ensuring that its annual budget represents a reasonable estimate of the costs of providing agreed service levels. It also holds appropriate balances and reserves so that resources are available to allow a managed and considered response should any significant variations or emergencies arise.

1.5 This report considers:

- The Council's financial governance regime
- The robustness of the budget
- Review of Earmarked Reserves
- Adequacy of General Fund balances.

2. FINANCIAL MANAGEMENT, BUDGETARY CONTROL, AND RISK MANAGEMENT

2.1 East Suffolk Council operates a comprehensive and effective range of financial management policies. These are contained in the Financial Procedure Rules, which form part of the Council's Constitution. This Constitution is available on the Council's website.

2.2 The Council conducts an annual review of the effectiveness of the system of internal control and reports on this in the Annual Governance Statement.

2.3 The Council continues to implement effective risk management policies, identifying corporate, operational and budget risks and mitigating strategies.

2.4 The internal and external audit functions play a key role in ensuring that the Council's financial controls and governance arrangements are operating satisfactorily.

2.5 This is backed up by the review processes of Cabinet, Scrutiny Committee, and the Audit and Governance Committee.

2.6 East Suffolk has a good record of budget and financial management and is expecting a balanced position for April 2021 to March 2022, although this is being achieved through some use of the In Year Savings Reserve. All relevant reports to Council, Cabinet, and Committees have their financial implications identified and the links to the Financial Sustainability theme of the East Suffolk Strategic Plan is outlined. Emerging budget pressures are kept under review during the year and this has been particularly important during 2020/21 with the financial impact of the Covid-19 pandemic.

2.7 Strategic risk management is embedded throughout the Council to ensure that all risks are identified, mitigated and managed appropriately. The Council's insurance arrangements are in the form of external insurance premiums and internal funds to self-insure some items.

2.8 Projects are subject to business case challenge on financial and risk matters and to reflect their importance in delivery of the East Suffolk Strategic Plan and achievement of Financial Sustainability.

2.9 Income assumptions, particularly on the Council's key income streams of Council Tax and business rates, are subject to continual review and are reported on a monthly basis on the Council's intranet.

2.10 It is imperative that the Council's commitment to strong financial governance is maintained and strengthened. During 2021/22, the Council will fully implement the CIPFA Financial Management Code, which is designed to set the standards of financial management for local authorities, support good practice in financial management, and assist local authorities in demonstrating their financial sustainability.

3. ROBUSTNESS OF THE 2021/22 ESTIMATES AND TAX CALCULATIONS

3.1 The Budget and Council Tax calculations for 2021/22 are based upon forecasts of expenditure, income and Council Tax revenues up to 31 March 2022, with some significant assumptions made in order to prepare these forecasts. When setting its Council Tax for 2021/22 the Council needs to be satisfied that these assumptions are reasonable. In order to ensure the robustness of the budgeting, the Council's budget process commenced in September 2020 and progressed with Cabinet's consideration of the MTFS and draft Budget in December 2020 and February 2021. Scrutiny Committee considered these in detail in December 2020 and January 2021.

3.2 All areas of budgets have been reviewed by Heads of Service. In addition, a number of budgets are subject to overall cross-service review, including the Council's employee budgets.

3.3 The pay award for staff from 1 April 2021 has not yet been agreed, however a 2% increase has been included in the estimates for 2021 to 2022. Reflecting staff turnover, an in-year vacancy allowance of £300k is maintained. Non pay related budgets have not been inflated unless there is a contractually committed rate of inflation where services can demonstrate a requirement to do so to maintain service delivery levels.

3.4 Budgeted increases for fees and charges are based on three key principles: cost recovery, market value and inflationary increases. The budget also includes those increases that are set and proposed by Government. The Sales, Fees, and Charges Lost Income scheme introduced by the Government in response to the pandemic has been extended into the first quarter of 2021/22, and this will be an important support underwriting income during this uncertain period.

3.5 Since March 2009 interest rates have continued to produce low returns from investments. In response to the Covid-19 pandemic, the Bank of England has reduced interest rates to historically low levels, with the minimum lending rate currently at 0.1%.This has been assumed as the base level of investment interest for 2021/22, although the Council's investments in pooled money market and property funds deliver returns of over 4%. Security of the Council's cash is the over-riding consideration in setting its Treasury Management Policy Statement. During the year the Council constantly receives advice from its Treasury Advisors with regard to the creditworthiness of financial institutions.

3.6 Business rates is a key income stream to the Council, particularly given that significant reform in the local government finance system which will include resetting business rates baselines that was intended for 2020/21 has now been further deferred until 2022/23. Reset of the system and the establishment of new funding formulae could result in the Council losing its financial advantage under the current system, which derives from the fact that actual business rates income is above the baseline in the system which was set at a low level in 2013/14. The Council's MTFS from 2022/23 onwards only includes business rate income at the government baseline level, assuming that the reset of the system will eliminate this current advantage in whole or in part, although this probably represents a worst-case scenario. Due to the impact of the Covid-19 pandemic on businesses, the position on business rates for 2021/22 is subject to a high degree of uncertainty, and a prudent and cautious approach has been taken to all elements of forecasting business rates income. The Government has introduced a Tax Income Guarantee Scheme which will reduce the impact of business rate income reductions in 2020/21, significantly assisting the position going into 2021/22.

3.7 Council Tax income has also been subject to financial impacts as a result of the pandemic, particularly in respect of the level of support reliefs and reduced collection. A Tax Income Guarantee Scheme and a Local Council Tax Support Grant have also been introduced and will provide valuable support, but a prudent approach has been adopted in setting the tax base for next year, which consequently shows a reduction on 2020/21. Covid-19 emergency grant funding also continues to provide important support to the Council's budget and pandemic response in 2021/22.

3.8 The Council is required to complete a range of calculations (Prudential Indicators) to evidence that borrowing for capital expenditure is affordable, prudent and sustainable over the medium term. This makes sure that the cost of paying for interest charges and repayment of principal by a minimum revenue contribution (MRP) each year is taken into account when drafting the Budget and Medium Term Financial Strategy.

4. ADEQUACY OF RESERVES AND BALANCES

4.1 The Council holds a very significant value of funds in reserves and balances to enable it to plan and manage its finances soundly. In addition to the Council's General Fund which will have a balance of £6 million as at 1 April 2021, the Council's earmarked reserves are estimated to stand at around £47 million going into next year, excluding £13 million held in the Business Rates Equalisation Reserve which is required to deal with the Business Rates Collection Fund deficit arising in 2020/21.

4.2 The Council has continued to develop its prudent financial management arrangements, through the development of earmarked reserves. Broadly speaking, the Council holds earmarked reserves to:

a) Comply with statutory requirements or proper accounting practice;

b) To mitigate potential future risks or smooth year-to-year fluctuations in income or expenditure;

c) To earmark resources for future spending plans or potential liabilities.

4.3 For the purposes of this report, around £20m, principally in the Business Rates Equalisation Reserve, is available in category b) above. This represents a very high level of coverage of risk and volatility in addition to the General Fund Balance, and enables the Council to plan over the medium term to achieve financial sustainability and ultimately balance the budget on an ongoing basis without recourse to the regular use of reserves.

4.4 As far as the General Fund Balance itself is concerned, the significant financial challenges and opportunities facing the Council over the medium term mean that the Council should continue to maintain a robust level of General Fund Balance of about 3% to 5% of budgeted gross expenditure, equating to about £4 million to £6 million.

4.5 The recommendation to maintain a General Fund Balance of £6 million is reinforced by review of the main budget risks and sensitivity to the Council's key in-year income and expenditure variables as shown below. Due to the ongoing effects of the Covid-19 pandemic, this assessment is more cautious than in previous years.

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Review & Risk Assessment of General Fund Revenue Balances 2021/22				
Risk Area	**Identified Risk**	**2021/22 £'000**	**Risk Likelihood / Sensitivity %**	**Risk Value £'000**
Pay Costs	Additional 1% on pay award	350	10%	35
Investment Income	Further Reduction in investment rates to 0%	650	10%	65
Car Parking Income	Further COVID-19 impacts above Government Support Levels	4,164	20%	833
Planning Fee Income	Further COVID-19 impacts above Government Support Levels	1,685	15%	253
Building Control Income	Further COVID-19 impacts above Government Support Levels	753	15%	113
Land Charges Income	Further COVID-19 impacts above Government Support Levels	415	25%	104
Garden Waste Income	Further COVID-19 impacts above Government Support Levels	2,448	40%	979
Waste Recycling Income	Possible decline in dry recyclables market	1,985	40%	794
Housing Benefit Subsidy	Possible adverse variance on subsidy	50,438	0.5%	252
Housing Benefit Overpayments	Possible adverse variance on overpayments recovered	1,314	25%	329
Council Tax Support	Possible increase in caseload - effect on tax base	1,626	10%	163
Homelessness Administration	Possible increased caseload resulting from economic factors and welfare changes	764	20%	153
Partnerships	Further Covid-19 Impacts especially on Leisure contracts	1,848	50%	924
Savings and Efficiencies	Non-achievement of vacancy saving	300	20%	60
Risk Value Sub Total				**5,057**
Add: Contingency for unforeseen factors				800
Total Risk Value				**5,857**

5. FUTURE YEARS BEYOND 2021/22

5.1 Changes to the Local Government Finance system from 2022/23 onwards will place significant pressure on the Council's financial position. The Council will need to respond in increasingly innovative ways through the Financial Sustainability theme of the East Suffolk Strategic Plan to support its communities and maintain the momentum towards this objective. This will need to be combined with robust budget management and full implementation of the CIPFA Financial Management Code. However, the Council has very significant levels of earmarked and general balances enabling it to manage key risks and deliver on a range of objectives, and plan over the medium term to achieve financial sustainability.

6. CONCLUSION

6.1 Overall, the estimates are robust, taking into account known risks and mitigating strategies, and the reserves are adequate for the 2021/22 Budget plans.

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Chief Finance Officer and Section 151 Officer

February 2021