APPENDIX G

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 21 February 2024.

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.

2. Role of the Chief Finance Officer

2.1 The statutory duties of the Chief Financial Officer are set out in the Finance Procedure Rules which form part of the Council's Constitution.

2.2 The Chartered Institute of Public Finance and Accountancy (CIPFA) published a Statement on the Role of the Chief Financial Officer in Local Government. The Statement sets out the five principles that define the core activities and behaviours that belong to the role of the Chief Finance Officer in public service organisations and the organisational arrangements needed to support them:

1. is a key member of the Leadership Team, helping it to develop and implement strategy and to resource and deliver the organisation's strategic objectives sustainably and in the public interest;

2. must be actively involved in, and able to bring influence to bear on, all material business decisions to ensure immediate and longer-term implications, opportunities and risks are fully considered, and alignment with the organisation's financial strategy

3. must lead the promotion and delivery by the whole organisation of good financial management so that public money is safeguarded at all times and used appropriately, economically, efficiently and effectively.

To deliver these responsibilities the Chief Finance Officer:

4. must lead and direct a finance function that is resourced to be fit for purpose; and

5. must be professionally qualified and suitably experienced.

2.3 This report considers:

- The Council's financial governance regime
- The robustness of the budget
- Review of Earmarked Reserves
- Adequacy of General Fund Balances
- Financial standing

3. Financial Management, Budgetary Control, And Risk Management

3.1 East Suffolk Council operates a comprehensive and effective range of financial management policies. These are contained in the Finance Procedure Rules, which form part of the Council's Constitution. This Constitution is available on the Council's website. These rules are regularly evaluated and reviewed in the light of operational considerations and changing circumstances. The Financial Procedure Rules were last amended in 2022/23 and are currently in the process of being reviewed again.

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

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

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

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

3.6 East Suffolk has a good record of budget and financial management and reports quarterly budget monitoring to the Corporate Leadership Team and Cabinet, and for the 2023/24 outturn the Council is expecting a small surplus.

3.7 All relevant reports to Council, Cabinet, and Committees have their financial implications identified and linked to the East Suffolk Strategic Plan. Emerging budget pressures are kept under review during the year and this has been particularly important in recent years, with the Covid-19 pandemic, high inflation and the cost of living crisis. This is in addition to operating in a local government environment with uncertainty of the scale and timing of funding reforms, and one year settlements. This leads to more prudent and cautious financial planning assumptions over the medium term.

3.8 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.

3.9 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.

3.10 Collection rates on the Council's key income streams of Council Tax and Business Rates, are monitored monthly via the Anglia Revenue Partnership (ARP) and inform the income planning assumptions for review and updates of the MTFS.

3.11 In October 2019, CIPFA published the Financial Management Code (FM Code), which provides guidance for good and sustainable financial management in local authorities and will provide assurance that authorities are managing resources effectively. The FM Code applies a principle-based approach which requires that a local authority demonstrates that its processes satisfy the principles of good financial management for an authority of its size, responsibilities and circumstances.

3.12 Using these standards, and key questions within the guidance, the Chief Finance Officer carried out a self-assessment of current processes, procedures, and governance arrangements, which was reported to the Audit and Governance Committee in December 2021. No areas were assessed as non-complaint. Demonstrating Value for Money and developing a Long Term Financial Strategy were areas identified for improvement. As noted above, in the absence of certainty of Local Government funding in the medium term, this makes longer term planning more challenging and a more prudent approach being taken.

4. Robustness Of The 2024/25 Estimates And Tax Calculations

4.1 The Local Government Act 2003 (Section 25) places a personal duty on the "Chief Financial Officer" (Section 151 Officer) to make a report to the Council about the robustness of the estimates made for the purposes of the Council Tax calculations and the adequacy of financial reserves and balances. The Act also requires the Council to have regard to the report before it makes its budget and Council Tax decisions. when it is considering its Budget and Council Tax. Where this advice is not accepted, it should be recorded formally within the minutes of the Council meeting.

4.2 The provisions of the Local Government Finance Act 1992 set out what the Council has to base its budget calculations upon and require the Council to set a balanced budget with regard to the advice of its Chief Finance Officer (Section 151).

4.3 The Budget and Council Tax calculations for 2024/25 are based upon forecasts of expenditure, income and Council Tax revenues up to 31 March 2025, with some significant assumptions made in order to prepare these forecasts. When setting its Council Tax for 2024/25 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 2023 and progressed with Cabinet's initial consideration of the MTFS on 7 November 2023 and the draft Budget on 2 January 2024. The Overview and Scrutiny Committee also considered the draft Budget on 18 January 2024.

4.4 The pay award for staff from 1 April 2023 was agreed at a flat rate increase of £1,925 for pay points up to scale point 43. Pay points above this level but below Chief Officer increased by 3.88%. Chief Officer pay increased by 3.5%. The mean percentage increase for the current year was 5.32% against a budget assumption of 4%. The budget assumption is for a 3% increase in 2024/25 and a 2% increase for 2025/26 onwards. Reflecting staff turnover, an in-year vacancy allowance of 4% of staffing costs is maintained.

4.5 The Council's financial strategy has previously assumed for a number of years that any inflationary pressures incurred on goods and services expenditure are contained within existing budgets, or through more efficient spending. The exceptions being utility costs, rates and specific contracts and agreements where inflation increases are built in. The impact of inflation is most evident in the Capital Programme, utilities and insurance premiums, and the Council's Operation services. Budget headings have been reviewed and revised as part of the budget process for 2024/25 where inflationary increases are evident.

4.6 Both pay and general inflation represent a continued risk to the Council's budget and MTFS. A contingency budget of £0.600m has been added into the budget for 2024/25 and each subsequent year of the MTFS to mitigate some of this potential risk.

4.7 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. However, in setting fees and charges for 2024/25, the Council has been mindful of the cost of living crisis and the ability to pay of the district's communities.

4.8 Interest rates have increased rapidly over the last couple of year in response to inflation. This has increasing investment interest returns to the Council which has benefited both the General Fund and Housing Revenue Account by providing significant additional income to the Council in the current year, above original estimates. The 2024/25 budget has assumed the Council will continue to benefit from higher interest rates with the interest income budget increased by £1.7m. This source of income is gradually reduced over the MTFS in anticipation of interest rates falling over, as the bank of England inflation target of 2% is reached.

4.9 Existing loans are all at fixed rates and therefore not susceptible to market increases. Where the Capital Programme requires future additional borrowing, the budget will be updated as and when projects are completed and actual borrowing is known.

4.10 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 and lending on the local authority market.

4.11 Business Rates is a key income stream to the Council. The budget estimate for Business Rates income for 2024/25 is based on the NNDR1 return completed at the end of January, and the budget has been uplifted by £3.271m from the original budget. This is due to a combination of the Chancellor increasing the standard multiplier for 2024/25 by 6.6% (payable by businesses with premises valued at more than £51,000), and a lower contribution to the provision for appeals. This improvement to the original budget for 2024/25 has been a significant item to addressing the initial budget gap.

4.12 Significant reform in the local government finance system which will include resetting Business Rates baselines has now been further deferred and unlikely to happen before 2026/27. Reset of the system and the establishment of new funding formulae is likely to result in the Council losing a degree of 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. In expectation of the impending reform, the approach that has been taken is to apply 2023/24 estimates to the 2025/26 budget onwards, with the exception being renewables and a tapering of the Pooling Benefit from £2.0m in 2025/26 to £1.0m in 2026/27 and then to £0.50m in 2027/28. This is to reflect a cautious approach to the overall Business Rates income position in the latter years of the MTFS. The MTFS assumption is that the Council will continue to retain 100% Business Rates income from renewables. If the current treatment of existing renewables is revised, any new renewable hereditaments coming online during the MTFS period will improve the forecast position.

4.13 Council Tax income was subject to financial impacts as a result of the pandemic, but also not to the extent that was previously anticipated. To a large extent, the position on the tax base returned to projected pre-pandemic levels. However, in-year monitoring of collection rates for 2023/24 are showing a fall in collection rates compared to the previous year, suggesting the cost of living crisis may now be impacting. The estimated taxbase growth for 2024/25 had fallen from 1.48% in 2023/24 to 0.75%. From 2025/26 a cautious approach continues to be taken to growth in the overall tax base and the MTFS assumes taxbase growth around half of the estimated growth for 2024/25 at 0.40%. This approach considers the impact of inflation and the cost of living crisis on development site completions, and Local Council Tax reliefs and collection rates.

4.14 East Suffolk Council created East Suffolk Services Limited (ESSL) to operate as a Local Authority Trading Company (LATCo) following a thorough review of its joint venture (JV) partnership with Norse, which ended on 30 June 2023. The initial focus of the Council and company has been to ensure a smooth transition of services from the JV to ESSL. Alongside focussing on this transition, ESSL's business plan for year 1 has also included supporting the workforce during this period of change, whilst understanding operationally the company's costs for delivering services on behalf of the Council. The first year's operation of ESSL has been and continues to be about stabilisation and identification of opportunities for the development and improvement of the various services this company delivers. As with other council services, ESSL has faced cost pressures such as increases in pay awards and fuel. This has contributed significantly to the required uplift in the company's base budget for 2024/25 and 2025/26 of £1.7m and £1.1m respectively. Year one of operation has also identified an under investment in the service for a number of years, which has added to the pressure on both the revenue and capital budgets for 2024/25.

4.15 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 payment (MRP) each year is considered when drafting the Budget and Medium Term Financial Strategy. The Council has a large and ambitious Capital Programme and external funding and the realisation of capital receipts and external funding will be important in ensuring affordability and delivery of the programme.

5. Adequacy of Reserves and Balances

5.1 The Council holds a healthy balance 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 2024, the Council's earmarked reserves are estimated to stand at around £39 million going into 2024/25.

5.2 Main budget risks and sensitivity to the Council's key in-year income and expenditure variables in 2024/25 are referred to below:

- Cost of living crisis impact, especially potential increases in homelessness and temporary accommodation costs

- Inflationary pressures
- Deliverability of large capital projects
- Local government pay award levels
- Financial pressures at a County Council level

5.3 In response to risk, sensitivity, and uncertainty, 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 and uncertainties and to smooth year-to-year fluctuations in income or expenditure;

c) To earmark resources for future revenue spending plans including delivery of the strategic plan and transformation projects;

d) To earmark resources to finance the Capital Programme, in particular short life assets; and

e) To hold grant funding received in advance of spend.

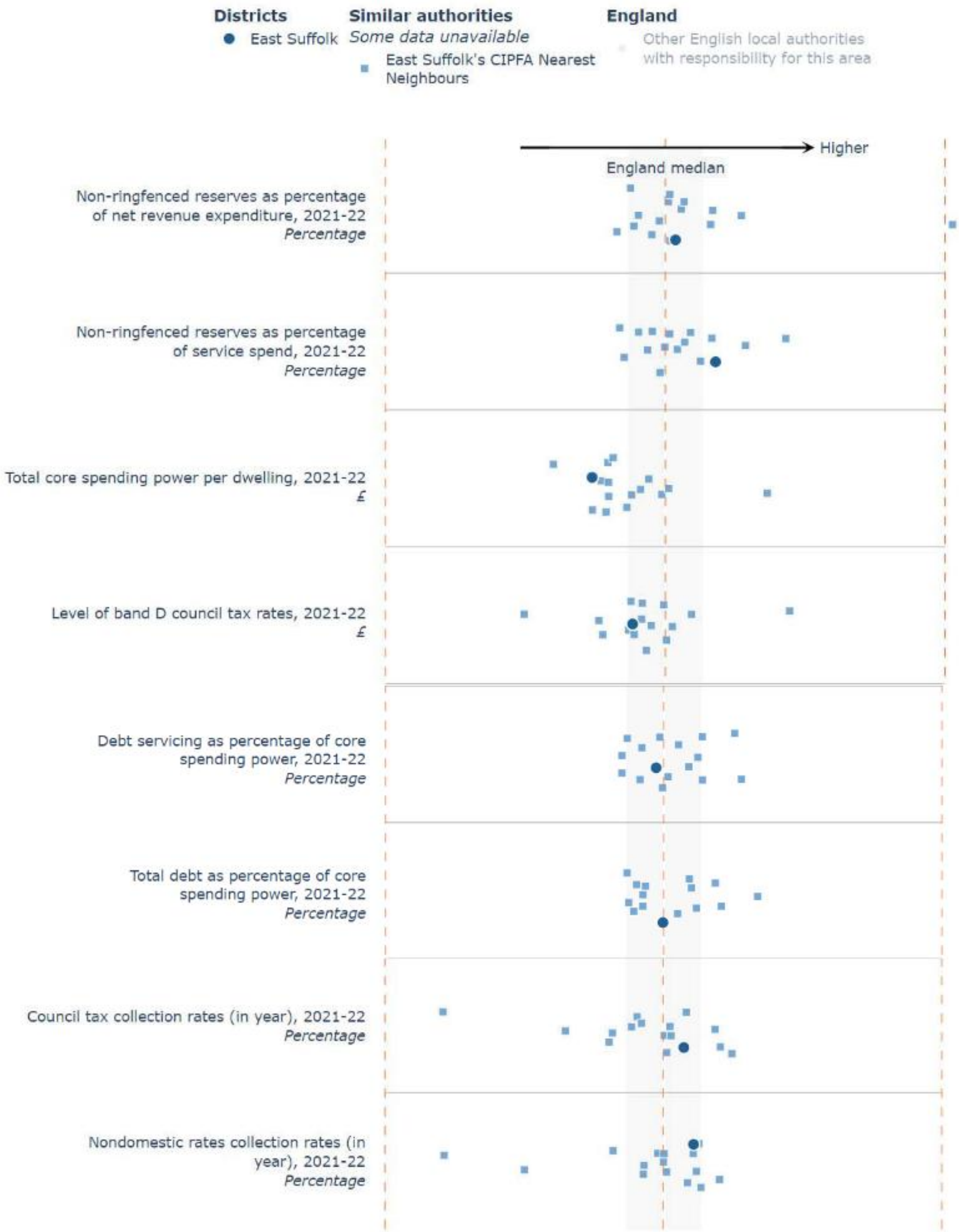
5.4 For the purposes of this report, around £14.5 million, principally in the Business Rates Reserves and the In-Year Savings Reserve, is available in category b) above. This represents around 20% of the net budget requirement before reserve movements - a high level of coverage of risk and volatility in addition to the General Fund Balance of £6 million.

5.5 As far as the General Fund Balance itself is concerned, the 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 (£150 million for 2024/25), equating to about £4.5 million to £7.5 million.

6. Financial Standing

6.1 During 2023/24, the Office for Local Government (Oflog) provided a new online tool to bring together a selection of existing metrics across a subset of service areas for data that is available at different levels of local authority. The aim is to provide authoritative and accessible data and analysis about the performance of local government and support its improvement. This tool is still in its early stages of development and the data needs to be treated with caution. Data on its own does not provide a complete picture and data may be inaccurate, incomplete or inconsistent for comparator authorities. The assessment of risk associated with an indicator may also be open to different interpretations.

6.2 There is one data set for Corporate and Finance and this provides contextual information and a sense of how a local authority operates. The latest available information is based on 2021/22. An extract is provided below.



6.3 The points below provide some brief narrative to explain the above, and supports the Council being in a good position with its overall reserve balance, servicing debt and collection rates for Council Tax and Business Rates.

- *Non-ringfenced reserves as percentage of net revenue expenditure* - East Suffolk has a value of 160.4%. The median value of East Suffolk CIPFA nearest neighbours for this measure is 152.8%.

- *Non-ringfenced reserves as percentage of service spend* - East Suffolk has a value of 184.6%. The median value of East Suffolk CIPFA nearest neighbours for this measure is 139.8%.

- *Debt servicing as percentage of core spending power* - East Suffolk has a value of 8.4%.The median value of East Suffolk CIPFA nearest neighbours for this measure is 10.6%. It should be noted that this indicator on its own, cannot show whether a local authority is managing its risks effectively or why the debt was incurred. Different debt will carry different risks and will be issued on different repayment terms.

- *Total debt as percentage of core spending power* - East Suffolk has a value of 449.2%. The median value of East Suffolk CIPFA nearest neighbours for this measure is 449.2%.

- *Council tax collection rates (in year)* - East Suffolk has a value of 97.9%. The median value of East Suffolk CIPFA nearest neighbours for this measure is 97.4%.

- *Non-domestic rates collection rates (in year)* - East Suffolk has a value of 98.2%. The median value of East Suffolk CIPFA nearest neighbours for this measure is 97.7%.

7. Future Years Beyond 2024/25

7.1 In recent years, the Council's financial position has been largely characterised by the fact that it has been in an advantageous position under the current Business Rates Retention system. Reforms to this system (and implementation of the Fair Funding Review) have been deferred on a number of occasions which has benefitted the Council and has enabled it to build up and maintain a robust reserves position. This will be important in enabling the Council to adjust to pressures and uncertainties in the medium term and to address underlying budget gaps going forward.

7.2 The forecast annual budget gap for 2025/26 is £5.40m and rising to £7.660m in 2025/26 and £8.38m in 2027/28. The Medium Term Financial Strategy currently forecasts increasing annual budget gaps in the medium term - £5.27m in 2025/26, £7.65m in 2026/27 and £8.37m in 2027/28. This reflects the uncertainty of local government finance reforms and the range and scale of expenditure and income pressures. A strategy for a combination of actions will be needed in the next budget round to ensure a longer term sustainable position; including a phased use of reserves, maximisation of income, and the achievement of savings. The Council's overall balance on reserves is currently healthy, which will provide the time for actions to embed and outcomes to be realised.

8. Conclusion

8.1 Overall, the estimates are robust, taking into account known risks and mitigating strategies, and the reserves are adequate for the 2024 to 2025 budget plans.

Lorraine Rogers (FCCA)

Chief Finance Officer and Section 151 Officer

February 2024