APPENDIX C

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 23 February 2022.

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. The Financial Procedure Rules are currently in the process of being reviewed and amended, with a view to a revised set of rules being in place for 2022/23.

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 2022 to March 2023. 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 over the last two years 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 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. Following on from the principles of the FM Code, there are 7 areas of focus, supported by a set of guidance standards against which Councils should be assessed.

2.11 Using these standards, and key questions within the guidance, the Chief Finance Officer has carried out a self-assessment of current processes, procedures, and governance arrangements, and this was reported to the Audit and Governance Committee in December 2021.

2.12 This self-assessment has rated the majority of standards to be fully compliant with no areas rated as non-compliant. Key questions that have been rated Amber and as areas for further development primarily involve the following:

- Demonstration of value for money.
- Revision of Financial Procedure Rules and associated training.
- Development of a Long-Term Financial Strategy and possible use of scenario planning.
- Development and embedding of options appraisal and business case methodology in projects.

3. ROBUSTNESS OF THE 2022/23 ESTIMATES AND TAX CALCULATIONS

3.1 The Budget and Council Tax calculations for 2022/23 are based upon forecasts of expenditure, income and Council Tax revenues up to 31 March 2023, with some significant assumptions made in order to prepare these forecasts. When setting its Council Tax for 2022/23 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 2021 and progressed with Cabinet's consideration of the MTFS and draft Budget in December 2021 and February 2022. Scrutiny Committee considered these in detail in December 2021 and January 2022.

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 for staff below Chief Officers level, however a 2% increase has been included in the estimates for 2021/22 and 2022/23. Reflecting staff turnover, an in-year vacancy allowance of £0.600m 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 was extended into the first quarter of 2021/22, and has been a useful support underwriting income during this period.

3.5 Since March 2009 interest rates have continued to produce low returns from investments. Interest rates have been at historically low levels, although the minimum lending rate has just been increased to 0.5% in response to inflation concerns. 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. Significant reform in the local government finance system which will include resetting Business Rates baselines has now been further deferred until 2023/24. Reset of the system and the establishment of new funding formulae is likely to 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 approach taken in the MTFS from 2023/24 onwards is to only include estimates of rates income and Section 31 Grant at baseline levels. However, a revision from the previous MTFS is a revised assumption that the Council will continue to retain 100% Business Rates income from Renewables and that various government funding streams in 2022/23 will continue in some form as part of the Fair Funding Review and associated transition arrangements. In 2021/22, Business Rates income has not been impacted by the pandemic as greatly as was initially feared, due to a combination of Government support to businesses through rate reliefs; legislation preventing certain appeals against rating valuations; and the ability of the economy to adapt to the circumstances of the pandemic.

3.7 Council Tax income has been 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 has returned to projected pre-pandemic levels.

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. The Council has a large and ambitious Capital Programme and external funding and the realisation of capital receipts will be important in ensuring affordability and delivery of the programme.

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 2022, the Council's earmarked reserves are estimated to stand at around £56 million going into next year. This overall balance on earmarked reserves includes;

- £14.9 million held in the Business Rates Equalisation Reserve which is required to deal with the Business Rates Collection Fund deficit arising in 2021/22, and
- £9.3 million held in the Covid Reserve. This reserve holds funding specifically received in response to Covid. This is to cover additional expenditure and to fund initiatives during the pandemic. The funding also includes Section 31 Grants associated with Business Rates Reliefs granted to retail, hospitality and leisure and nurseries. This Grant funding is released into the General Fund to fund the Business Rates Collection Fund deficit accounted for in 2022/23 and 2023/24.

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 £20 million, 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. This assessment continues to adopt a cautious approach due to continuing spend and income pressures associated with the pandemic.

Review & Risk Assessment of General Fund Revenue Balances 2022/23				
Risk Area	**Identified Risk**	**2022/23 £'000**	**Risk Likelihood / Sensitivity %**	**Risk Value £'000**
Pay Costs	Additional 1% on pay award	300	30%	90
Supplies and Services	Inflationary pressure on supplies and services	736	30%	221
Car Parking Income	Post pandemic recovery	4,836	15%	725
Planning Fee Income	Post pandemic recovery	1,785	15%	268
Building Control Income	Post pandemic recovery	775	15%	116
Land Charges Income	Post pandemic recovery	203	15%	30
Garden Waste Income	Post pandemic recovery	2,532	15%	380
Waste Recycling Income	Possible decline in dry recyclables market	2,400	15%	360
Housing Benefit Subsidy	Possible adverse variance on subsidy	41,008	0.5%	205
Housing Benefit Overpayments	Possible adverse variance on overpayments recovered	1,314	20%	263
Council Tax Support	Possible increase in caseload - effect on tax base	1,679	10%	168
Homelessness Administration	Possible increased caseload resulting from economic factors and welfare changes	976	20%	195
Partnerships	Inflation and pay pressures, rising energy costs at leisure centres	2,759	50%	1,380
Savings and Efficiencies	Non-achievement of savings	1,174	20%	235
Risk Value Sub Total				**4,636**
Add: Contingency for unforeseen factors				1,350
Total Risk Value				**5,986**

5. FUTURE YEARS BEYOND 2022/23

5.1 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 a significant underlying budget gap. It is now increasingly likely that reforms to the Local Government finance system will be implemented in 2023/24 and although the position following that is extremely uncertain, it is clear that over the next few years the Council will need to focus on achieving financial savings and maximising income to adapt to reduced levels of resources whilst still delivering on Strategic Plan objectives.

6. CONCLUSION

6.1 Overall, the estimates are robust, taking into account known risks and mitigating strategies, and the reserves are adequate for the 2022/23 Budget plans.

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Chief Finance Officer and Section 151 Officer

February 2022