SELBY
DISTRICT COUNCIL

Report Reference Number: C/20/10

To:	**Council**
Date:	**18 February 2021**
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Title: **The Budget, Reserves and Balances 2021/22**

Summary: **This report confirms the robustness of the Council's budget and the adequacy of its reserves and balances having regard to a variety of factors.**

Recommendations:

It is recommended that councillors consider the Chief Finance Officer's statements in paragraphs 2.7 and 2.13 when setting the Council Tax.

Reasons for recommendation

To provide Council with assurance on the proposed budget and the Council's reserves in order to formally set the budget and Council Tax for 2021/22.

1. Introduction and background

1.1 Section 25 of the Local Government Act 2003 requires the Chief Finance Officer to make a formal report to the Council on the robustness of the budget and adequacy of reserves.

1.2 The last year has been a year like no other with the Covid-19 pandemic having profound impacts on all aspects of our lives. For the Council, this has been a year of rapid change as we moved to home working, carrying out our business remotely where possible and playing our part in the response to the virus, whilst still delivering the vital public services our communities rely on. Then add to this the prospect of Local Government Re-organisation (LGR) in North Yorkshire and we have a "perfect storm".

1.3 We have seen heightened financial risk - with additional workload and costs, significant income losses and delays to planned savings initiatives, all as a direct result of the impacts of the virus, as we have moved in and out of national lockdowns and local restrictions. And we have major uncertainty over our future.

1.4 In September 2020 Council approved a revised estimate for 2020/21 and a revised Medium-Term Financial Strategy, to ensure the financial capacity was and is in place to support our response and manage services effectively as we emerge from the pandemic and negotiate our way through LGR.

1.5 Additional Covid related funding from central government has been welcomed but has not been sufficient to fully cover our costs and losses to date and the Council has had to draw on its own reserves – reserves established to manage financial risk, although no-one could have anticipated the magnitude of this risk.

1.6 It is against this backdrop that the budget for 2021/22 has been formulated – a budget for a time of unprecedented risk and uncertainty.

2. The Report

Robustness of the Budget

2.1 Whilst Covid is impacting in many service areas during 2020/21, for the most part service budgets have been reviewed on the assumption of a 'normal year' for 2021/22. In some cases however, where on-going impacts are clear, then budgets have been revised using best available assumptions. Investment income is one such budget where the low bank rate is expected to remain for the next 2/3 years.

2.2 Financial plans include cautious assumptions on service income (for example recycling and planning income) and include provision for rises in demand led services such as waste and recycling; and the Housing Revenue Account includes provision for a CPI +1% increase in rent levels. Cost pressures from changes in Government Policy and increasing demand for services will continue to be closely monitored and will be managed through the Council's revenue reserves in the short to medium term and base budget savings plans for the longer term. Over the next 2/3 years the medium-term financial position will be kept under continuous review.

2.3 For the immediate future the proposed budget includes one-off contingencies to help manage the risks associated with Covid-19 and LGR – including £150k for LGR, £500k staffing contingency to deal with service backlogs, and £1.5m Covid contingency to manage service pressures. These are in addition to the annual operational and commissioning contingencies.

2.4 The Council's Financial Strategy and Medium-Term Financial Plan (3 year budget) have been refreshed to take account of the 2021/22 provisional local government finance settlement. The funding from central Government relating to the Business Rates Baseline (£2.274m safety net plus £128k cap compensation multiplier) will be £2.402m for 2021/22. The 2021/22 Finance Settlement shows an increase of £1.6m to settlement funding (including Rural Services Delivery Grant, Lower Tier Service Support Grant, Covid emergency funding and New Homes Bonus). Whilst 2021/22 is a relatively positive settlement with some significant one-off increases, the ongoing impacts of the virus are still not known and beyond 2021/22 we await the outcome of the fairer funding review, the review of the business rates retention system and also a review of new homes bonus. The current MTFS and budget assumes that new Homes Bonus is phased out over the next 3 years.

2.5 Looking ahead, the Government's plans for LGR will undoubtedly impact on Local Government in North Yorkshire but until a decision on future structures is taken budgets have been constructed assuming a 'going-concern'. The Council's reserves provide resources to mitigate any impacts in the short to medium-term and the level and profile of the required savings will be kept under review as the longer term financial outlook beyond 2021/22 becomes clearer.

2.5 The forecast savings requirement by 2023/24 is circa £3m for the General Fund, although the budget recognises that with capacity diverted to the Council's Covid response, savings of this level will not be achievable within the required timescales. Accordingly the budget applies reserves to bridge the funding gap in the short to medium-term.

2.6 There is risk to the Council's share of Business Rates income although a large surplus on our Business Rates Collection Fund is forecast for 2021/22 as a result of the windfall from renewable energy. In accordance with the approved MTFS the budget transfers the related surplus funds to reserves but given the risks to expenditure and income and delays to savings as a result of Covid, the budget allocates them to support the revenue budget. Looking forward it is expected that these receipts will cease following the reset of business rates baselines and therefore they are not assumed within our recurring resources.

2.7 In respect of the proposed Council Tax requirement for 2021/22, councillors are asked to consider the following statement:

" The Chief Finance Officer reports that the estimates of income and expenditure forming the Council's General Fund Revenue and Housing Revenue budgets for 2021/22 have been prepared on the basis of existing plans, known commitments and the financial implications of the proposals for savings and where necessary, service development and improvement. Where it has been necessary to do so, in the case of certain budgets such as contract payments, investment income and income from fees and

charges, assumptions have been used for inflation, interest rates and demand for services which are considered to be reasonable and prudent. In addition a risk assessment is undertaken for these budgets and contingencies are available to mitigate the risk within the budget. In view of this, the Chief Finance Officer considers the Council's budget estimates for 2021/22 to be robust."

Reserves and Balances

2.8 As with most local authorities, the Council maintains a range of reserves and balances to help manage its finances over the medium to longer term. These can be analysed into three main types:

i) General Fund (Working) Balance – comprises of a non-earmarked balance (currently set at a minimum of £1.5m) which is set aside to cover the risk of excess inflation or unforeseen events;

ii) Housing Revenue Account - as with the General Fund balance but this time relating to a local authority's housing function whilst it operates a Housing Revenue Account. The minimum balance is currently set at a £1.5m, which is set aside to cover the risk of excess inflation or unforeseen events within the HRA service;

iii) Specific reserves – amounts earmarked for specific items of expenditure to meet known or predicted liabilities and future investment.

2.9 Appendix A provides an assessment of the appropriate level of balances for the General Fund and HRA. Appendix F of the Budget and Council Tax report next on this agenda shows the estimated balance on each reserve at the end of 2020/21 after taking into account the impact of the agreed budget and provides a brief summary of the purpose of each reserve.

The General Fund (Working) Balance

2.10 As indicated above, the General Fund Balance is an un-earmarked balance. Following a review of the adequacy of this balance there are no proposals to change the minimum of £1.5m. The approved Medium Term Financial Strategy recognises that use of reserves to support day to day service costs is unsustainable and therefore the routine use of General Fund Balances stopped with effect from 2013/14.

Housing Revenue Account Balance

2.11 The current minimum balance on the Housing Revenue Account is £1.5m which equates to £494 per property as at 1 April 2019 and is considered to be sufficient to cover a reasonable level of risk within the HRA.

Specific Earmarked Reserves

2.12 In relation to reserves set aside for specific items of expenditure, a review has also been conducted to determine adequate levels. Given the heightened risk to the Council's finances as a result of Covid, an additional £8m plus a further £9.2m has been earmarked in the Business Rates Equalisation Reserve to support the revenue budget. This forms part of the Council's recommendations on the use of these reserves to support the 2021/22 revenue budget and capital programme and programme for growth proposals are included with the budget report.

2.13 In respect of the adequacy of the Council's proposed financial reserves and balances councillors are asked to consider the following statement:

"The Chief Finance Officer reports that, having conducted a review of the Council's requirement for the minimum working balance, taking into consideration various matters including:-

- **the Council's spending plans for 2021/22 and the medium term financial position;**
- **a risk assessment of the main items of income and expenditure;**
- **a risk assessment of the savings plan;**
- **adequacy of estimates of inflation, interest rates;**
- **treatment of demand led pressures;**
- **the need to respond to emergencies including the on-going response to Covid-19, and**
- **other potential calls on balances.**

Therefore a minimum amount of £1.5m for the General Fund balance and a minimum of £1.5m for the Housing Revenue Account are considered adequate for this purpose.

The Chief Finance Officer also reports that the Council's earmarked reserves have been reviewed as part of the Medium Term Financial Strategy and Medium Term Financial Plan and with the proposals included within the budget, remain adequate."

3. Legal/Financial Controls and other Policy matters

3.1 Legal Issues

3.1.1 This report complies with Section 25 of the Local Government Act 2003, which requires the Chief Finance Officer to make a formal report to the Council on the robustness of the budget and adequacy of reserves.

3.2 Financial Issues

3.2.1 There are no financial implications as a direct result of this report. CIPFA's Financial Resilience Index identifies a range of financial indicators and assess their relative risk when compared to other authorities. Generally, the indicators suggest Selby is 'lower risk' but unallocated reserves are considered high risk. In isolation unallocated reserves are relatively low but this should be seen in the context of the Council's overall reserves position – earmarked reserves are used to manage financial risk. The latest published index relates to 2018/19 with a further update anticipated by the end of February 2021.

3.2.2 CIPFA have also introduced a new Financial Management Code which becomes mandatory from 1 April 2021. Audit and Governance Committee received an assessment of Selby's arrangements at thir October 2020 meeting. Although Selby is largely compliant with the Code, some actions for improvement have been identified. Covid-19 has delayed progress against the agreed actions but this will be monitored by the Committee during 2021/22.

4. Conclusion

4.1 Whilst there is much uncertainty around the on-going impacts of the pandemic, the Council's 2021/22 budgets are robust, and based on current assumptions and assessed risk, the Council has adequate levels of reserves and balances, however given expected levels of Government funding, increases to the Council's cost base and delays to savings, a drawdown from reserves will needed during 2021/22.

5. Background Documents

Budget reports to and associated minutes of the Executive

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Appendices:
Appendix A – Review of General Fund and HRA Balances

APPENDIX A

Review of General Fund and HRA Balances

Introduction

1. The Chartered Institute of Public Finance and Accountancy (CIPFA) believes that Local Authorities, on the advice of their Chief Finance Officer, should make their own judgements on such matters taking into account all the relevant local circumstances. Such circumstances vary, and there is a broad range within which authorities might reasonably operate depending on their particular circumstances.

2. There is no definitive guidance as to the minimum level of balances or reserves, either as an absolute amount or as a proportion of expenditure, since each local authority is independent, operates in a unique local environment and the decision is one of a number of inter-related decisions taken as part of its financial strategy. Section 32 of the Local Government Act 1992 requires billing authorities (such as Selby) to have regard to the level of reserves needed for meeting estimated future expenditure when calculating the budget requirement. Budgets are based upon forecasts of pay and price inflation, changes in interest rates, and the demand for and levels of service to be provided. The existence of balances provides for unexpected changes from these forecasts. Consequently, the provision of an appropriate level of balances is a fundamental part of prudent financial management over the medium and longer term and with the events of 2020 the need for adequate reserves to cope with significant unforeseen challenges has never been more important.

3. The Council has a well established and robust reserves strategy – earmarking resources to manage risk, cover commitments and support investment/service improvement. Annual amounts are set aside to cover known commitments over their expected ‘whole life’. The Business Rates Equalisation Reserve is the main earmarked reserve established to support the revenue budget, leaving general balances as funding of last resort.

Principles to Assess the Adequacy of Reserves

4. Setting the level of general reserves is just one of several related decisions in the formulation of the Medium Term Financial Strategy and the budget for a particular year. Account should be taken of the key financial assumptions underpinning the budget alongside a consideration of the authority's financial management arrangements. In addition to the cash flow requirements of the authority, the following factors should be considered:

Budget Assumptions

- Wider economic impacts of national policy changes (such as Brexit) on inflation, interest rates and supply chain prices
- treatment of inflation and interest rates
- a risk assessment of the main items of income and expenditure
- Staff turnover rates and appropriate level of salary vacancy factor
- estimates of the level of and timing of capital receipts and general cashflows
- treatment of demand-led pressures (e.g. take-up of housing benefits and Council Tax Support)
- treatment of planned efficiencies and savings
- financial risks inherent in significant funding partnerships, contracts or major capital developments
- the availability of other funds to deal with major contingencies and the adequacy of provisions

Financial Standing and Management

- the overall financial standing of the authority
- the authority's track record in budget and financial management
- the capacity to manage in-year budget pressures
- the strength of financial information and reporting arrangements
- the authority's financial procedure rules and budgetary flexibility
- the adequacy of insurance arrangements to cover major unforeseen risks

Use of any "excess" balances

5. Any use of excess balances (i.e. those above the agreed minimum working balance) needs to be carefully considered in association with the Council's Medium Term Financial Strategy. Balances are a finite resource and can only be used once. Any application of balances should be focused on support for short-term budget restructuring and not ongoing 'base' items of expenditure. Ideally balances should be used to fund one-off expenditure, time-limited expenditure or 'invest to save' type spending.

The impact of the reductions in public sector funding will require significant savings to be made and there is an on-going risk that sufficient savings will not be delivered within the required timescales – reserves and balances would have to be used to bridge any gap between net spending and grant.

What is an appropriate level of Balances for Selby District Council?

<u>General Fund</u>

6. The current Council policy is for the General Fund Balance to be a minimum £1.5m. This represents approximately 12.3% of net service expenditure.

- *Adequacy of inflation*

Generally budgetary provision is made for inflation in respect of pay, prices and contract expenditure (in 2021/22 a 2% allowance for pay inflation has been included within the budget) although the government has indicated public sector pay restraint. It remains unclear what the impact on the Council will be as a result of the withdrawal from the EU. Although the pandemic is overshadowing many aspects of the economy, some level of economic volatility would be reasonable to expect and there may be impacts as suppliers seek to recover additional costs from their customers. Reserves are available to support the revenue budget in the short to medium term. An adverse variance of 1% in the assumptions made to these forms of expenditure would result in additional expenditure of approximately **£200k** in any one year.

- *Adequacy of interest rate assumption*

The Council is a net lender. An adverse variance of 0.25% in interest rates would increase the budgeted expenditure by approximately **£100k.**

- *Treatment of demand led pressures*

Demand volatility can affect both expenditure (e.g. housing benefit claims or property growth in our waste collection service) and income (e.g. number of planning applications). Housing Benefits are a significant item of expenditure estimated at approximately £13m in 2021/22 the majority of which is met by government subsidy. The estimate of subsidy is complex and is therefore relatively 'high risk'. There had also been a number of regulatory changes in recent years affecting the take up and it is considered prudent therefore to allow for some fluctuation in the net cost of benefits either reflecting subsidy variations, demand changes and changes in regulations. A figure of **£100k** is considered adequate for this purpose.

Provision for growth within our street scene service has been incorporated into the revenue budget.

With regard to income from fees and charges the major income budgets are those relating to:

- Trade waste
- Car Parks
- Planning
- Land Charges
- Industrial Unit Rents
- Court Costs
- Lifeline
- Leisure contracts

There is a high risk that expected income will not materialise due to the on-going effects of the virus.

Leisure services have been severely impacted during 2020/21 with closure of Summit Indoor Adventure and our leisure centres.

Some significant income losses/service subsidies are included within the budget but a fall in demand beyond that predicted for 2021/22 of say a further 10% would lead to a reduction in income of around **£500k**.

- *Responding to emergencies*

Examples include flooding, and the outbreak of foot and mouth disease. As a local authority, the Council can, in certain cases, gain protection through the Government's Bellwin Scheme although it is prudent to allow for expenditure which would not be covered by the scheme – for example the fire at Great Heck in 2015/16. A figure of **£300k** is considered adequate to cover for emergencies.

- *Savings delivery*

The Council has a strong track record for savings delivery but as the target increases it becomes more challenging to deliver. Furthermore with capacity diverted towards the Council's response to Covid-19 delays to savings are expected. The Business Rates Equalisation Reserve includes monies set aside to back-fill the Council's savings plan should this not be delivered as quickly as planned. At the end of 2020/21 the balance on this reserve is forecast to be £4.8m and a further £15.0m (net of drawdown) is to be added to this reserve in 2021/22 - overall this is considered sufficient to mitigate this risk over the medium term without drawing on general balances.

- *Other Issues*

The Council also has an unusually large Non Domestic Rate debit to collect due to the power industries. The timing of receipts and any changes in debit could have a major impact on the Council's cash flow and Business rates income. The current Business Rates Retention scheme guarantees a level of income for the Council through 'safety net' arrangements leaving around £180k funding at risk for the coming year. As highlighted above, at the end of 2020/21 the Council will have circa £4.8m set aside in the Business Rates Equalisation Reserve which is considered sufficient to mitigate this risk over the medium term.

Taking all of these factors into account it would be prudent to maintain the current policy of holding minimum General Fund balances of £1.5m. This combined with the Council's internal financial controls and other earmarked reserves should ensure the authority recognises financial 'issues' early and has the capacity to respond accordingly.

HRA

7. The Housing Revenue Account (HRA) minimum working balance is currently £1.5m which equates to £497 per property at 1 April 2020 which represents 17.2% of the net HRA budget. The estimated HRA balance at 1 April 2021 is projected to be £1.5m.

A £75k contingency is included within the HRA budget. An assessment has been made of the HRA budgets which are subject to external influence. This assessment includes the impact of additional expenditure against revenue budgets, variations in the capital programme, the impact of limiting growth bids, reduced income collection rates and an assessment of risk of the age of the stock and vulnerability for repairs planned for future years having to be brought forward.

- *Adequacy of inflation*

Generally budgetary provision is made for inflation in respect of pay, prices and contract expenditure (in 2021/22 a 2% allowance for pay inflation has been included within the budget). An adverse variance of 1% in the assumptions made to these forms of expenditure would result in additional expenditure of **£60k** in any one year.

- *Treatment of demand led pressures*

Demand volatility can affect expenditure (e.g. requests for housing repairs). Housing repairs are a significant item of expenditure estimated at £2.6m in 2021/22. The age of the stock and winter weather conditions affects the need for repairs year on year. It is considered prudent therefore to allow for some fluctuation in the cost of repairs. A figure of **£300k** is considered adequate for this purpose.

- *Capital Programme*

The HRA has a substantial capital programme each year. This is based on an estimate of the amount of work and costs at a point in time. Until the programme commences and a full assessment is made of properties in the relevant element of the programme there is a degree of uncertainty to the volume of work. In addition until the contract for the works is let the costs can only be estimated. It is considered prudent to allow for some fluctuation in the capital programme for additional costs through either additional works or costs or both. A figure of **£300k** is considered adequate for this purpose.

The capital programme is spread across a number of years and elements of the programme due to resources available will be deferred until later years this in itself carries a risk that works may need to be undertaken sooner than expected or that the cost of repairs increases until such time as a particular element of the programme is delivered. It is considered prudent to allow for some fluctuation in the capital programme. A figure of **£500k** is considered adequate for this purpose.

- *Other Issues*

The value of bad debts requiring write off within the HRA is currently rising due to the current economic climate. These bad debts are met from HRA income. It is considered prudent to allow for some fluctuation in bad debts levels. A figure of **£300k** is considered adequate for this purpose.

Taking all of these factors into account it would be prudent to maintain the current policy of holding minimum HRA balances of £1.5m. This combined with the Council's internal financial controls should ensure the authority recognises financial 'issues' early and has the capacity to respond accordingly.