

## **Section Three – Robustness of Estimates and Adequacy of Reserves**

### **Background**

1. As part of its budget setting processes, the council has a duty to consider the adequacy of its reserves and working balances. Under Section 25 of the Local Government Act 2003 the Section 151 Officer is required to state in the budget report their view on the robustness of estimates for the coming year, the medium term financial strategy and the adequacy of proposed reserves and balances.
2. This report provides a summary of the review of reserves and working balances undertaken this year which will form part of the considerations around budget setting for 2021-22.

### **Reserves Policy**

3. The council has developed a Reserves Policy which documents how it will manage and utilise its financial reserves in meeting the financial challenges it faces over the medium term. This is reviewed annually, with the current version dated January 2021 this can be found at Appendix 6a.

### **Assurances**

4. With regard to assessing the robustness of the budget, assurances have been sought of the following:-
  - The financial planning process for 2021/22
  - The financial strategy, including the Medium Term Financial Plan
  - Clear monthly budget monitoring by Heads of Service
  - Effective risk based internal and external audits reporting through the Finance and Audit Committee.
  - Effective corporate and operational risk management arrangements

### **Principles to assess risk in relation to the Adequacy of Usable Reserves**

5. In order to assess the adequacy of usable reserves when setting the budget for the General Fund the Director (Corporate Services), as S151 Officer, has considered the risks facing the General Fund and future investment requirements in capital and other projects. This information has been supplemented with consideration of the council's financial management and control arrangements, the national political and economic situation, advice from professional bodies and reserve practices of other like authorities to derive the recommended level of working balances and reserves for the 2021-22 financial year.

### **Assessing the risks**

6. As in previous years a risk assessment has been undertaken which attempts to quantify the risks to the Council's financial position in the forthcoming financial year for the General Fund. The outcomes of this assessment can be found at Appendix 6b.

## **Consideration of the council's financial management and control arrangements**

7. In preparing the detailed budget for 2021-22, the Finance Team has engaged with budget holders and their services to ensure that the budget is based on realistic estimates of income, expenditure and liabilities.
8. The council has in place a continual process for reviewing and adjusting its budget during the financial year. Monthly budget monitoring reports are presented to budget holders for review and comment. All reports to the Corporate Management Team and Members for decision are required to consider financial implications so that these can be properly understood and captured in the decision-making process. On a quarterly basis formal budget monitoring reports are produced and considered by the Corporate Management Team and Members to enable the reporting of budget variances over £10,000 and to provide the mechanism to call to account budget holders where this is appropriate.
9. In October 2019, Full Council adopted a new Corporate Plan for the period 2019 to 2023 which set the direction and guiding principles for council activity during the period to deliver a Gravesham to be proud of. The Corporate Plan recognises the need for the council to work differently to enable it to deliver more homes, more jobs and more investment in the borough. In doing this, the council will need to continue its activity to move away from reliance on funding from Central Government and become more commercial in some of the activity it undertakes.

## **National Considerations**

10. Local government has experienced a sustained period of financial uncertainty and significant change. This uncertainty relates to the overall UK economy, COVID-19 impacts, as well as the impact of national policy changes. There has also been a lack of clarity regarding the way in which local government is funded in the medium to long term. This year like last year central government has issued a one year settlement which covers 2021-22. The Government intends to review how business rates income is to be distributed and various other schemes such as the fair funding review. It therefore remains uncertain how this will impact the Council in the coming years. The proposed budget takes into account information currently available.

## **Professional advice**

11. Guidance received from the Audit Commission in 2012 indicated that, in the Commission's view, a prudent level of working balances was to retain an amount equivalent to three months net revenue spending requirement. For the General Fund, three months net spending would equate to approximately £3 million.

## **Movement in Working Balances and Reserves**

12. Analysis of movements in working balances and reserves have been considered and are set out in the next table. It is considered that all movements are managed movements and have been reported to senior management and Members through the council's budget monitoring arrangements.

|  | Projected<br>Balance as<br>at<br>31/03/2021<br>£(000) | Balance as<br>at<br>31/03/2020<br>£(000) | Balance as<br>at<br>31/03/2019<br>£(000) | Balance as<br>at<br>31/03/2018<br>£(000) | Balance as<br>at<br>31/03/2017<br>£(000) |
|--|---|--|--|--|--|
| General Fund Minimum Working<br>Balance    | £2,000  | £2,000                                   | £1,250                                   | £1,250                                   | £1,250                                   |
| General Fund General<br>Reserve            | £3,250  | £3,250                                   | £4,000                                   | £4,000                                   | £2,000                                   |
| Usable Working<br>Balances                 | £3,924  | £5,101                                   | £4,038                                   | £2,055                                   | £2,912                                   |
| <b>Total</b>                               | <b>£9,174</b>   | <b>£10,351</b>                           | <b>£9,288</b>                            | <b>£7,305</b>                            | <b>£6,162</b>                            |
| Net Annual Movement increase /<br>decrease | <b>-£1,177</b>  | £1,063                                   | £1,983                                   | £1,143                                   | £67                                      |
| Other Earmarked<br>Reserves                | £13,353   | £10,041                                  | £9,419                                   | £5,761                                   | £4,228                                   |
| Revenue Grants<br>Unapplied                | £1,021  | £1,865                                   | £1,819                                   | £1,737                                   | £2,833                                   |
| <b>Total</b>                               | <b>£14,374</b>  | <b>£11,906</b>                           | <b>£11,238</b>                           | <b>£7,498</b>                            | <b>£7,061</b>                            |
| <b>Net Annual Movement</b>                 | <b>£2,468</b>   | <b>£668</b>                              | <b>£3,740</b>                            | <b>£437</b>                              | <b>£349</b>                              |

### Assessing the appropriateness of Working Balances and Reserves

13. The minimum prudent level of reserves is a matter of judgement and is the council's safety net for any unforeseen expenditure or other circumstances. The current Medium Term Financial Strategy contains the core principle to preserve a total minimum level of £2m General Fund working balances, with a further £3.25m General Revenue Reserve to enable the Council to meet unforeseen challenges or pressures on its financial position.
14. Based on the assessed risks at the time of making the assessment of General Fund Working Balances in relation to setting the budget for 2021-22, it is the view of the Director (Corporate Services) that the minimum of £5.25m in General Fund working balances should be retained during 2021-22.
- a minimum working balance of £2m to assist cash flow.
  - £3.25m General Revenue Reserve to enable the Council to meet unforeseen challenges or pressures on its financial position.
15. In respect of Earmarked Reserves, the table below sets out the opening balance and forecast balances to 31/03/2021.

| <b>General Fund Earmarked Reserves</b>         | <b>Opening Balance<br/>01/04/2020<br/>£'000</b> | <b>Forecast Use of Reserve<br/>(Expenditure)<br/>£'000</b> | <b>Forecast Contributions<br/>(Income)<br/>£'000</b> | <b>Forecast Balance<br/>31/03/2021<br/>£'000</b> |
|--|---|--|--|--|
| Planning Policy Reserve                        | 369   | (280)  | 50   | 139  |
| Asset Enhancement Reserve                      | 1,320   | (864)  | 100  | 556  |
| Spend to Save Reserve                          | 160   | (162)  | 2  | --   |
| Leisure Centres Reserve                        | 1,649   | (399)  | 359  | 1,609  |
| Corporate Priorities Reserve                   | 250   | (24)   | --   | 226  |
| Town Pier Pontoon Reserve                      | 111   | (24)   | 12   | 99   |
| Local Authority Mortgage Scheme (LAMS)         | 25  | (25)   | --   | --   |
| Elections Reserve                              | 74  | --   | --   | 74   |
| NNDR Collection Fund Equalisation Reserve      | 500   | --   | 4,406  | 4,906  |
| IT Infrastructure Reserve                      | 340   | (284)  | 75   | 131  |
| DSO Vehicle Capital Reserve                    | 102   | (360)  | 289  | 31   |
| Freighter Replacement Reserve                  | 1,002   | (400)  | 221  | 823  |
| NNDR Growth Fund Reserve                       | 588   | (280)  | 239  | 547  |
| Lower Thames Crossing Reserve                  | 150   | (10)   | --   | 140  |
| Woodville Repairs Reserve                      | 227   | (50)   | 57   | 234  |
| Investment Interest Equalisation Reserve       | 500   | --   | --   | 500  |
| Housing & Commercial Growth Fund               | 700   | --   | --   | 700  |
| St George's Income Protection Reserve          | 948   | --   | --   | 948  |
| Commercial Income Protection Reserve           | 483   | --   | 211  | 694  |
| Service Review Reserve                         | 241   | (208)  | --   | 33   |
| Playgrounds Reserve                            | 117   | --   | --   | 117  |
| Decriminalisation Reserve                      | 185   | (75)   | 100  | 210  |
| Enterprise Reserve                             | --  | (349)  | 500  | 151  |
| Climate Change Reserve                         | --  | (15)   | 500  | 485  |
| <b>Sub-total - Specific Earmarked Reserves</b> | <b>10,041</b>                                   | <b>(3,809)</b>   | <b>7,121</b>   | <b>13,353</b>                                    |
| Revenue Grants not yet applied                 | 1,865   | (844)  | --   | 1,021  |
| <b>Total - All Earmarked Reserves</b>          | <b>11,906</b>                                   | <b>(4,653)</b>   | <b>7,121</b>   | <b>14,374</b>                                    |

16. The finance team have taken a pragmatic approach this year and have focused on the review of the larger reserves that the authority holds. It is the opinion of the Director (Corporate Services) that all existing earmarked reserves should be retained, with the exception of the Local Authority Mortgage Reserve, which is to be closed at the end of 2020-21, having served its purpose.
17. The increase in the NNDR collection fund equalisation reserve relates to Business Rates reliefs that have been paid from the collection fund and the need to safeguard the additional Section 31 grants received in 2020/21. The Collection Fund deficit will be repaid in 2021/22 using this reserve.
18. By making these changes, it is the view of the Director (Corporate Services) that the General Fund continues to maintain adequate reserves and working balances and that the budget proposals recommended to Cabinet are robust and sustainable. The risk assessment conducted does, however, set out a number of areas of risk or uncertainty and, for this reason, the reserves and working balances maintained for the General Fund will be kept under review.

**Opportunity Cost of holding reserves**

19. Having set minimum levels, the opportunity cost of holding reserves needs to be considered. All balances are used to either reduce temporary borrowing or are invested subject to other cash flows. Therefore in measuring any opportunity cost of holding these reserves, account needs to be taken of the interest saving. The opportunity cost of holding the reserves is therefore a judgment whether the 'worth' of expenditure foregone is more than the income generated. Given the current economic climate and prevailing uncertainty over future funding it is considered that the risks the authority is exposed to exceed the opportunity cost of holding reserves.