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 2022-23.

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 at Appendix 4a.

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

4. In order to assess the adequacy of usable reserves when setting the budget for the Housing Revenue Account (HRA), the Director (Corporate Services) has considered the risks facing the HRA 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 2022-23 financial year.

Assessing the risks

5. 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 Housing Revenue Account. The outcomes of this assessment can be found at Appendix 4b.

Consideration of the council's financial management and control arrangements

6. In preparing the detailed budget for 2022-23, the Financial Services Team has engaged with budget holders and their services to ensure that the budget is based on realistic estimates of income, expenditure and liabilities.

7. 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.

8. 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.

National Considerations

9. Local government has experienced a sustained period of financial uncertainty and significant change. This uncertainty relates to the overall UK economy as well as the impact of national policy changes, which have particularly affected the HRA around rent levels in previous years.

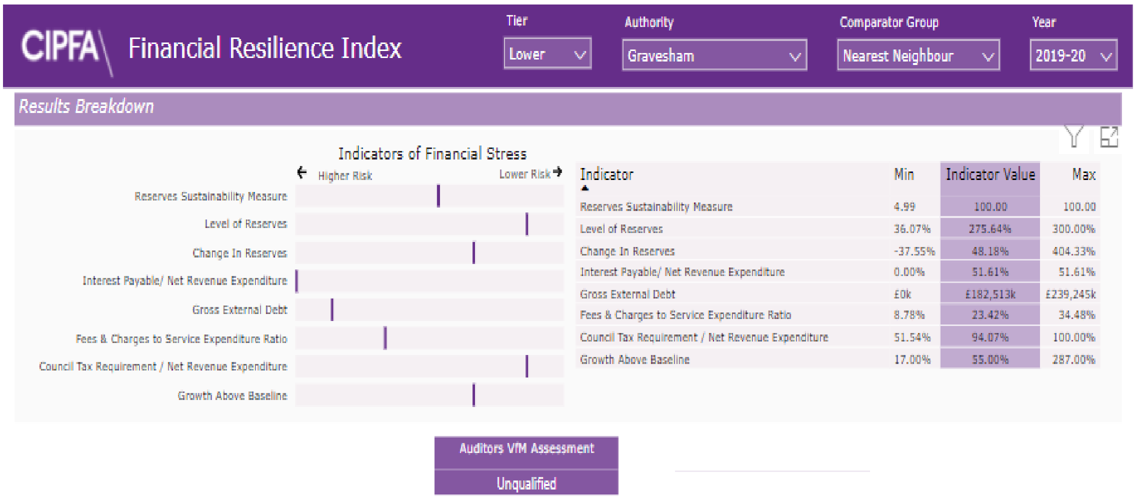
10. In November 2020 the Ministry of Housing, Communities and Local Government published the Social Housing White Paper 'The Charter for Social Housing Residents'. The Charter sets out the actions the government will take to ensure that residents in social housing are safe, are listened to, live in good quality homes, and have access to redress when things go wrong.

11. There remains uncertainty around the ongoing impacts of COVID-19 on council finances, the finances of tenants and delivering planned projects. This will be closely monitored during the coming year.

Professional advice

12 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 HRA, three months net spending would equate to approximately £4 million.

13. The Financial Resilience Review 2015 conducted by Grant Thornton recognises the importance of working balances and earmarked reserves as a means of providing a buffer against unplanned financial shocks and to invest in capital and other projects, including the funding of transformation. This view was shared by CIPFA in their briefing on English local authority reserves published in June 2015 and the Financial Resilience Index first published in December 2018, which contains indicators relating to the level of reserves an authority holds and the extent to which reserve are being utilised. The latest index shown in the table below shows data for the 2019-20 financial year.



Movement in Working Balances and Reserves

14. In furtherance of this analysis, movements in working balances and reserves have been considered and are set out in the next table. This indicates a positive trend in maintaining the level of working balances of the HRA. Whilst the analysis shows year-on-year reductions of the balance within the HRA General Reserve, these have been managed movements and have been reported to senior management and Members through the council's budget monitoring arrangements.

	Projected Balance as at 31/03/22 ('000s)	Balance as at 31/03/2021 ('000s)	Balance as at 31/03/2020 ('000s)	Balance as at 31/03/2019 ('000s)	Balance as at 31/03/2018 ('000s)	Balance as at 31/03/2017 ('000s)
HRA Mininmum Working Balance	3,000	3,000	3,000	3,000	3,000	3,000
HRA General Reserve	2,017	2,763	3,038	6,085	7,441	4,621
Total	**5,017**	**5,763**	**6,038**	**9,085**	**10,441**	**7,621**
Net Annual Movement (+ represents an increase in balance)	- **747**	- **274**	- **3,047**	- **1,356**	**2,820**	

Benchmarking

15. Benchmarking was undertaken to consider the relative positions of the minimum working balances retained by the authorities in England assessed as being the most similar to Gravesham Borough Council and other Kent stock holding authorities. This identified that the level of minimum level of working balances retained by this authority (at £3m), is higher than most. It is important to note, however, that Gravesham has a larger housing stock than all other comparators, with Gravesham's housing stock at 31 March 2021 standing at 5,642. The review also recognises that each authority will structure their reserve arrangements differently and will be affected to a greater or lesser relative degree by the risks outlined in the risk assessment at Appendix 4b, as well as differing net revenue budget requirements and policies around how they establish contingency amounts.

Assessing the appropriateness of Working Balances and Reserves

16. The introduction of self-financing to the Housing Revenue Account (HRA) in April 2012 fundamentally changed the way that local authority housing is funded. All rental income is retained locally in return for the authority taking on a level of debt representative of the value of the stock. The level of debt taken on by Gravesham

Borough Council amounted to £106 million, and at the end of 2021-22 will stand at £68m. A further £10m debt will be taken on during 2021-22 in relation to the New Build Programme taking the total debt as at the end of 2021-22 to £81m.

17. Business planning is central to a self-financed HRA to inform financial and service planning and managing risk. The business plan shows how over 30 years the rental and other income will fund all the investment needs of the stock, servicing of the debt and day-to-day management and repair requirements. It is the main tool for the financial management of the HRA and has a substantial impact on the asset management plans.

18. However, with 30 year business planning and the undertaking of £106 million of long-term debt/financing comes an increased risk to the authority of being unable to meet annual debt repayment obligations and the demands of managing around 5,642 council homes. The roll out of the Full Service for Universal Credit commenced in May 2018 and the council has experienced growing financial pressures for the council, and to residents in receipt of benefits. The on-going financial impact due to COVID-19 pandemic on our tenants is unknown. However, the council will continue to offer this support to its tenants in 2022-23 while continuing to make a distinction between those who cannot pay, and those who will not pay. The budget for 2022-23 reflects the potential effect of the pandemic on the rental income stream for the HRA and this will be reviewed during the course of the year with updates provided through quarterly budget monitoring arrangements

19. After considering the risks set out at appendix 4b to this report, professional advice and reserve practice of other comparator authorities it is the opinion of the Director (Corporate Services), that the minimum level of working balances be retained at £3 million. It is also considered that no changes are required to HRA reserves. The Housing Revenue Account 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, activity has already commenced to review future budgetary provisions and capital programme requirements to identify opportunities to sharpen and test future expenditure plans to inform future planned borrowing decisions.

Opportunity Cost of holding reserves

20. 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 grant funding it is considered that the risks the authority is exposed to exceed the opportunity cost of holding reserves.