

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

### **Section 25 Report**

#### **1. Background**

- 1.1. As part of its budget setting processes, the council has a duty to consider the adequacy of its reserves and working balances.
- 1.2. 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.
- 1.3. Section 26 of the same Act places an onus on the council to ensure that it has established a minimum level of reserves to be retained to cover any unforeseen demands that could not be reasonably defined within finalising the proposed budget.
- 1.4. This report sets out the view of the Director (Corporate Services) as S151 Officer pertains to the 2023-24 budget process and provides consideration of the budget proposals and the financial risks facing the council, alongside a summary of the review of reserves and working balances undertaken.

#### **2. Financial Planning and Budget Development Arrangements**

- 2.1. In assessing the budget proposals, assurances have been sought of the robustness of the financial planning process for 2023-24 and the council's longer term financial strategy, including the Medium Term Financial Plan, and the effectiveness of budget monitoring arrangements.

##### Financial Governance Arrangements

- 2.2. The Constitution of the Council specifically defines the role of all Members in setting the Council's Policy Framework and determining each year the Council's revenue and capital budget and Council Tax levy. Budget proposals are prepared by the Political Administration and approved for presentation to Full Council by the Cabinet. To support Members in fulfilling their role in determining the budget, draft budget proposals are presented and discussed in public by the Cabinet prior to approval, with Member Briefings held ahead of the formal Budget Setting meeting to enable all Members to obtain an understanding and ask questions on the budget proposals being made.
- 2.3. The council's Financial Procedure Rules are also contained within the Constitution, providing a documented framework for management of the Council's financial affairs.
- 2.4. Assessment has been made of the council's financial management arrangements against the Chartered Institute of Public Finance Accountants (CIPFA) Financial Management Code. The Code is designed to support good practice in financial management and to assist local authorities in demonstrating their financial sustainability. Review of the self-assessment undertaken during January 2023 has confirmed that the council continues to be fully compliant with the code.

- 2.5. The council can demonstrate a track record of strong financial management. Between 2016 and 2019 the council proactively progressed a number of workstreams to actively manage the council's finances during this period due to austerity and cuts to local government funding. In ratifying the budget for 2020-21, the Council was able to demonstrate delivery of activity totalling £4.25m which placed it in a position where it could demonstrate financial sustainability across the plan period at that time to 2028-29, with no additional savings required.
- 2.6. The current MTFs sets out activity delivered by the council during 2022-23 and what it will be required to deliver to maintain financial sustainability against the further challenges to the council's financial position. The budget proposals for 2023-24 include delivered activity of £1,425,040 in response to these challenges.

#### Financial Planning Process

- 2.7. The 2023-24 budget proposals and Medium-Term Financial Plan have been prepared during a period of extreme uncertainty and volatility. The central government announcement on the provisional finance settlement was not made until the 19 December 2022, policy guidance has provided a limited level certainty of the funding principles to be adopted for 2024-25 and confirmed that local government funding reform will not be implemented until 2025-26 at the earliest, the start of the next Comprehensive Spending Review period. This provides a challenging backdrop to develop long-term financial plans and a situation where much of the council's budget for 2023-24 was developed without knowing what the likely provisional settlement from government for the year would be.
- 2.8. This situation is compounded by the current state of the UK economy, the legacy impacts of the COVID-19 pandemic (particularly on major income streams such as car parking) as well as uncertainty on national policy affecting local government. The council has been transparent on how these factors have and are likely to place pressure on its financial position, with reports presented to Cabinet in May 2022 and October 2022 alongside updates included in quarterly budget monitoring reports received by both Cabinet and the Finance and Audit Committee.
- 2.9. The Council adopted its Medium Term Financial Strategy (MTFS) covering the period 2022-23 to 2026-27 in February 2022 which sets out how the council will plan for and meet the financial challenges it faces over the medium term as a means of delivering a robust and stable financial basis on which to deliver quality council services. Whilst the principal tenets of the MTFS remain relevant, the scale of the financial challenge has significantly increased over the last year, from an estimated £3m in February 2022, to £4.6m in October 2022. Without the proactive delivery of some of the initiatives set out in the MTFS the council would now be facing a budget gap in the region of £6m instead of the £4.37m currently forecast for 2026-27.
- 2.10. The Medium Term Financial Plan (MTFP) continues to provide the numerical representation of the council's future financial plan projections, based on the principles within the MTFS. The council has in place a continual process for reviewing and adjusting its budget and the assumptions contained within the MTFP during the financial year. Monthly budget monitoring reports are presented to budget holders for review and comment to ensure financial risks and pressures are highlighted at the earliest opportunity, ensuring a considered and planned response in developing any remedial action required. 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 publicly by 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.

### Budget development

- 2.11. The 2022-23 General Fund revenue budget represented a balanced budget position. In accordance with the objective in the council's Medium Term Financial Strategy and the latest assessment of the level of working balances and reserves, a sum of £1,453,370 was released from Excess Usable Working Balances to support the annual revenue budget for the year.
- 2.12. Budget monitoring to the end of Quarter Three has indicated that the council will overspend in 2022-23, by £1,446,810.
- 2.13. In preparing the detailed revenue budget for 2023-24, 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 future liabilities, with a sharpened focus on areas of high value and high risk. This has been particularly pertinent given the volatility in expenditure, in demand for services in certain areas, in income levels the council is able to generate from fees and charges, rental income and investment returns and the uncertainty around levels of central government funding for local government.
- 2.14. In the same way, additional scrutiny has been applied to capital project proposals given the limited resources the council has to fund such projects from its cash reserves and external sources of funding. All capital projects requiring external borrowing have been subject to specific decision papers supported by financial modelling with decisions to proceed only taken if there is evidence to support that each is a financially viable project.
- 2.15. Capital programme slippage has increased in recent years, due in particular to the increase in programme items relating to property assets and regeneration exposing the council to the current challenges in the construction industry around labour and material supply chains. Programme slippage could result in changes to borrowing repayment profiles included in the MTFP as well as increasing the borrowing costs required to be met from future income streams. During 2022-23 the council has developed more robust arrangements to ensure cash flow projections are provided for each project and are updated at least quarterly to enable spend and borrowing profiles to be more effectively managed and any finance cost impacts to be known earlier.
- 2.16. The proposed General Fund revenue budget for 2023-24 sets out a planned level of expenditure during the year which is greater than then level of annual funding and income the council is projected to receive. To achieve a balanced budget, £2,262,090 of Excess Usable Working Balances will be required to support the annual revenue budget for the year. Whilst this is affordable for 2023-24, moving forward the council cannot sustain this as level of drawdown from Working Balances as a long-term means of balancing its budget and decisive action must be taken during 2023-24 to ensure that the council lives within its means. The Balancing the Budget plan, set out in the Medium Term Financial Strategy, must be delivered to address this.
- 2.17. In setting the budget it is accepted that there will need to be some assumptions made regarding expected levels of service demand and spend assumptions, alongside cost recovery expectations and other opportunities for income generation. This year is more challenging than would normally be experienced, particularly given the number and nature of external factors the council is required to consider as part of the budget setting process. The annual assessment made of the adequacy of reserves and working balances is performed to ensure that, as far as is possible, the council has adequate reserves should any of these risks materialise.

### 3. Assessment of Working Balances and Reserves

- 3.1. The council maintains a Reserves Policy which sets out how the council will manage and utilise its financial reserves in meeting the financial challenges it faces over the medium term as a means of providing a robust and stable financial basis on which to deliver quality council services. The current Reserves Policy reflects the council's intention to ensure that its financial planning arrangements go beyond single year budget horizons and can be found at Appendix 6a.
- 3.2. The council maintains three types of reserves within its General Fund for the following purposes:
- a working balance to help cushion the impact of uneven cash flows and avoid the need for temporary borrowing.
  - a general reserve to provide a contingency to cushion the impact of unexpected events or emergencies.
  - earmarked reserves to meet known or predicted requirements or future liabilities.
- 3.3. As part of the budget setting process a review working balances and reserves is conducted to ensure that reserves are still appropriate and confirm the value at which reserves and working balances should be held.

#### General Fund Working Balance

- 3.4. The minimum prudent level of working balance for a council is not legislated; it is a matter of professional judgement and intended to be the council's mechanism for maintaining a stable cashflow position and managing unanticipated fluctuations in income and expenditure. The current Medium Term Financial Strategy contains the core principle to preserve a total minimum level of £2m General Fund working balances.

#### General Reserve

- 3.5. The level at which the General Reserve should be held is also not prescribed but is intended to be reflective of the council's assessment of its need for a safety net to provide for any unforeseen expenditure or other circumstances. The current Medium Term Financial Strategy contains the core principle to preserve a total £3.25m General Revenue Reserve.

#### Assessment of risks to the General Fund

- 3.6. To assess the adequacy of the General Fund Working Balance and General Reserve, the Director (Corporate Services), as S151 Officer, has considered the risks facing the General Fund and future investment requirements in capital and other projects. The risk assessment attempts to quantify the risks to the Council's financial position in the forthcoming financial year for the General Fund which have not been financially provided for, either within the proposed budget or an earmarked reserve. The outcomes of this assessment can be found at Appendix 5b.

#### Movement in the General Fund Working Balance and General Reserve

- 3.7. Analysis of recent movements has been conducted and is set out in the next table. This indicates that the council has maintained its minimum working balance and general reserve position in previous years and has been able to increase the level of Usable

Working Balances it has available. This has enabled the council to in recent years in terms of increasing the level of working balances of the General Fund. It is considered that all movements within earmarked reserves and application of revenue grants are managed activity and have been reported to senior management and Members through the council's budget monitoring arrangements.

	Projected Balance as at 31/03/2023 £(000)	Balance as at 31/03/2022 £(000)	Balance as at 31/03/2021 £(000)	Balance as at 31/03/2020 £(000)	Balance as at 31/03/2019 £(000)
General Fund Minimum					
Working Balance	£2,000	£2,000	£2,000	£2,000	£1,250
General Fund General Reserve	£3,250	£3,250	£3,250	£3,250	£4,000
Usable working balances	£4,264	£6,699	£6,033	£5,101	£4,038
Total	£9,514	£11,949	£11,283	£10,351	£9,288
Annual Net Movement increase / decrease	-£2,435	£666	£932	£1,063	£1,983

	Projected Balance as at 31/03/2023 £(000)	Balance as at 31/03/2022 £(000)	Balance as at 31/03/2021 £(000)	Balance as at 31/03/2020 £(000)	Balance as at 31/03/2019 £(000)
Earmarked Reserves	£8,171	£10,216	£16,585	£10,041	£9,419
Revenue Grants Unapplied	£868	£1,723	£2,494	£1,865	£1,819
Total	£9,039	£11,939	£19,079	£11,906	£11,238
Net Annual Movement increase /decrease	-£2,900	-£7,140	£7,173	£668	£3,740

\* Movement in other earmarked reserves due, in part, to recognition of business rate grants received by the council in respect of other preceptors being transferred to the Collection Fund.

- 3.8. The MTFP for 2023-24 has been prepared on the basis of continuing to draw on the usable working balances held by the council to meet in year expenditure, with £2,262,090 being drawn down to produce the balanced budget proposed for the 2023-24 financial year in addition to the amount forecast for 2022-23.
- 3.9. Whilst it is recognised that the building up and use of working balances is a key part of effective medium-term financial planning, such balances are only able to be used once. It is important to recognise that using working balances to support ongoing expenditure will only postpone the need for base budget reductions and not remove the need for this activity to take place; therefore, delivery of the Balancing the Budget plan set out within the MTFS is critical to ensure the ongoing financial sustainability of the council.

#### Specific Earmarked Reserves

- 3.10. The council holds a number of provisions, known as specific earmarked reserves, to enable it to effectively plan for known or predicted financial requirements or future liabilities that the council will need to meet. The next table sets out the opening balance and forecast balance of currently held reserves to 31/03/2023.

<b>General Fund Earmarked Reserves</b>	<b>Opening Balance 01/04/2022 £'000</b>	<b>Forecast Use of Reserve (Expenditure) £'000</b>	<b>Forecast Contributions (Income) £'000</b>	<b>Transfers Between Reserves £'000</b>	<b>Forecast Balance 31/03/2023 £'000</b>
Planning Policy Reserve	599	(226)	50		423
Asset Enhancement Reserve	977	(481)	100		596
Leisure Centres Reserve	47	(47)			--
Corporate Priorities Reserve	587	(67)			520
Town Pier Pontoon Reserve	136	12		(148)	--
Elections Reserve	137	(5)	35		167
NNDR Collection Fund Equalisation Reserve	2,188	(841)	91		1,438
IT Infrastructure Reserve	252	(170)	125		207
DSO Vehicle Capital Reserve	441	(458)	132		115
Freighter Replacement Reserve	1,032	(98)	221		1,155
NNDR Growth Fund Reserve	510	(287)	369		592
Lower Thames Crossing Reserve	140	(50)			90
Woodville Repairs Reserve	240	(175)	57		122
Investment Interest Equalisation Reserve	500				500
Housing & Commercial Growth Fund	700				700
Commercial Income Protection Reserve	661		97		758
Playgrounds Reserve	204	(160)	69		113
Decriminalisation Reserve	269	(269)			--
Enterprise Reserve	173	(358)	350		165
Climate Change Reserve	423	(61)		148	510
<b>Sub-total - Specific Earmarked Reserves</b>	<b>10,216</b>	<b>(3,741)</b>	<b>1,696</b>	<b>--</b>	<b>8,171</b>
Revenue Grants not yet applied	1,723	(855)			868
<b>Total - All Earmarked Reserves</b>	<b>11,939</b>	<b>(4,596)</b>	<b>1,696</b>	<b>--</b>	<b>9,039</b>

3.11. A full review of the specific earmarked reserves held by the council has been conducted as part of the budget setting process. Based on this review, the anticipated movements for some reserves have been adjusted across the MTFP period to reflect the latest assumptions around events that are likely to trigger a need to use specific reserves. The review has confirmed that all existing specific earmarked reserves should be retained, with the exception of the following: -

- **Town Pier Pontoon Reserve** - on 4 January 2022 the Cabinet made a decision to sell to the Town Pier and Pontoon, and the sale was completed in November 2022. The reserve is therefore no longer be needed and, in accordance with the decision by Cabinet, the remaining balance in this reserve will be transferred to the Climate Change Reserve to support the Council's Climate Change Strategy and initiatives.

#### 4. Conclusion

- 4.1. Based on the review findings contained within this report, it is the view of the Director (Corporate Services), as Section 151 Officer, that the budget estimates are robust and the current level of working balances and reserves are adequate. This view has been taken considering the opportunity cost of holding amounts in working balances and reserves and is based on the budget as proposed by the Administration, including the assumption that Gravesham Borough Council's Council Tax Levy is increased up to but not exceeding the referendum threshold set in place by the Secretary of State, resulting in a Band D council tax increase of £6.48 relating to the Gravesham Borough Council element of the charge in 2023/24.
- 4.2. Council Tax is the council's main source of income for funding services. Any lowering of the charge proposed will create additional pressure on the council's financial position, detrimentally impacting on the council's financial sustainability over the longer term and will widen the existing funding gap of £4.37m in 2026/27, requiring base budget reductions beyond those contained within the budget setting report.
- 4.3. It is my view that the budget proposals strike a prudent balance between the council continuing to fulfil its statutory requirements and maintaining its longer-term financial sustainability. Delivery of the Balancing the Budget plan of activity contained within the updated MTFs is not without its risks and will require unity of effort and difficult decisions to be taken regarding how the council operates and delivers services to the borough and its residents in the future. This said, the council's track record in delivering on such action and strong financial governance arrangements mean the council is well placed to respond effectively to these requirements.