

## **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 2024-25 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 2024-25 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 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. Since March 2020 the council has been responding to further funding pressures alongside managing the consequences of the COVID-19 pandemic and other macroeconomic factors affecting both the council and the communities it serves. The council has regularly and publicly reported its financial position, which has been supplemented in recent years with commentary on the financial pressures directly impacting the council. The latest of these reports was presented to the [Cabinet](#) in November 2023 and was complimented by briefing sessions with both Political Groups, to ensure clarity and transparency of the financial situation at the time and ahead of going into budget setting for the 2024/25 financial year.
- 2.7. The current Medium Term Financial Strategy 2022-23 to 2026-27 sets out the activity that is planned to be delivered to maintain financial sustainability against the further challenges to the council's financial position. The need to deliver against this Strategy has never been so clear. The budget proposals for 2024-25 include delivered activity of £1.81m in response to these challenges.

#### Financial Planning Process

- 2.8. The 2024-25 budget proposals and Medium-Term Financial Plan have been prepared during a period of continuing uncertainty and volatility.
- 2.9. The central government announcement on the provisional finance settlement was not made until the 18 December 2023, there is no certainty of the funding principles to be adopted for 2025-26 and it has been 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 difficult backdrop against which to develop any long-term financial plans and gave rise to a situation where much of the council's budget for 2024-25 was developed without knowing what the likely provisional settlement from government for the year would be.
- 2.10. The ability of the council to effectively construct future financial plans is further compounded by the current state of the UK economy and political uncertainty as the country heads into a General Election during 2024, with current political focus on near-term improvements to the economy. Short-term and tightening funding settlements, alongside higher levels of inflation and the increasing costs of delivering services, such as support to those finding themselves homeless, is creating real pressures on the council and the local government sector as a whole, which has been widely covered by the Media in recent times.
- 2.11. The Council adopted its Medium Term Financial Strategy (MTFS) covering the period 2022-23 to 2026-27 in February 2022, setting out how it 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.
- 2.12. During the last year the council has delivered a significant level of base budget reductions, albeit cost pressures continue to be present. The council's level of annual expenditure continues to exceed anticipated income and working balances have been significantly depleted in recent years. It is therefore imperative that the council works at a faster pace to ensure that it delivers base budget reductions and is able to maintain a level of working balances that continue to provide some protection against the impact of unexpected events or emergencies.

2.13. 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.

2.14. In the last year the council has further developed its treasury and cashflow management activity to further strengthen its financial governance arrangements, improve financial planning processes and enable assessment of the longer term implications of decisions taken by the council.

#### Budget development

2.15. The 2023-24 General Fund revenue budget showed planned expenditure for the year as being greater than expected income, requiring £2.07m of Working Balances to be used to produce an overall balanced budget. This will completely use up the Usable Working Balances currently held by the council and also require £1.14m to be used of the council's General Reserve, intended to provide a safety net to the council for any unforeseen expenditure or other circumstances.

2.16. Budget monitoring to the end of Quarter Three has indicated a small underspend for the council of £124,790. This is an improved position from Quarter Two and is driven principally by revised expected income from the Business Rates Retention Scheme (now that the consequences of the 2023 Revaluation exercise are clearer), a projected in-year salary underspend and the realisation of proactive budget rationalisation work the council is undertaking to balance its budget.

2.17. In preparing the detailed revenue budget for 2024-25, 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 and demand for services in certain areas against the expected levels of income 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.

2.18. Robust 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 was a financially viable project at the time; in some instances consideration has been given to 'pause' projects to protect the council's cashflow position and manage its borrowing position.

- 2.19. 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 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. These arrangements continued during 2023-24 and will be maintained for the future.
- 2.20. As previously referenced, the proposed General Fund revenue budget for 2024-25 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, £2.07m of will be required to be drawn from Working Balances to support the annual revenue budget for the year. Action has been taken during 2024-25 to proactively respond to the council's financial position and whilst the level of drawdown from working balances is affordable for 2024-25, moving forward the council cannot sustain drawdown from Working Balances as a long-term means of balancing its budget. The Balancing the Budget plan, set out in the Medium Term Financial Strategy, must be accelerated and delivered to address this.
- 2.21. 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 5a.
- 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. This is equivalent to 13.70% of the council's net budget requirement for 2024-25 but is currently projected to have reduced to 6% of the council's net budget requirement by the end of 2025-26, just above the level which the council's external auditor, Grant Thornton, considers a council to be at risk of financial failure.

#### 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.

	Balance 31/03/2020 £'000s	Balance 31/03/2021 £'000s	Balance 31/03/2022 £'000s	Balance 31/03/2023 £'000s	Projected Balance 31/03/2024 £'000s
General Fund Minimum Working Balance	2,000	2,000	2,000	2,000	2,000
General Fund General Reserve	3,250	3,250	3,250	3,250	3,250
Usable Working Balances	3,685	4,008	4,122	2,569	932
<b>Total</b>	<b>8,935</b>	<b>9,258</b>	<b>9,372</b>	<b>7,819</b>	<b>6,182</b>
Net Annual Movement Increase/(Decrease)	(353)	323	114	(1,553)	(3,190)

	Balance 31/03/2020 £'000s	Balance 31/03/2021 £'000s	Balance 31/03/2022 £'000s	Balance 31/03/2023 £'000s	Projected Balance 31/03/2024 £'000s
Earmarked Reserves	10,041	16,585	10,216	10,998	7,759
Revenue Grants Unapplied	1,865	2,494	1,723	1,468	978
<b>Total</b>	<b>11,906</b>	<b>19,079</b>	<b>11,939</b>	<b>12,466</b>	<b>8,737</b>
Net Annual Movement Increase/(Decrease)	668	7,173	(7,140)	527	(3,202)

The tables above show re-stated balances for Usable Working Balances following the revised accounting arrangements for the St George's Shopping Centre transaction. These are still subject to the external audit process and any amendment will be reported to Members.

- 3.8. The MTFP for 2024-25 has been prepared on the basis of continuing to draw on usable working balances held by the council to meet in year expenditure, with £2.07m 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. Continued reliance on Working Balances is not an option and is considered as an extremely short-term and risky strategy, leaving the council in a position where it is less able to manage the impact of any significant or unexpected events or emergencies during 2024-2025. Without further intervention, the council will not be able to set a balanced budget for 2025-26. 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 31/03/2024.

General Fund Earmarked Reserves	Opening Balance 01/04/2023 £'000	Forecast Use of Reserve (Expenditure) £'000	Forecast Contributions (Income) £'000	Transfers Between Reserves £'000	Forecast Balance 31/03/2024 £'000
Planning Policy Reserve	545	(232)	50		363
Asset Enhancement Reserve	988	(807)	100	122	403
Leisure Centres Reserve	28	(28)			--
Corporate Priorities Reserve	600	(385)	121		336
Elections Reserve	225	(163)			62
NNDR Collection Fund Equalisation Reserve	2,102	(721)			1,381
IT Infrastructure Reserve	457	(34)	25		448
DSO Vehicle Capital Reserve	344	(246)	132		230
Freighter Replacement Reserve	1,156	(800)	221		577
NNDR Growth Fund Reserve	408	(180)			228
Lower Thames Crossing Reserve	140	(140)			--
Woodville Repairs Reserve	122	(57)	57	(122)	--
Investment Interest Equalisation Reserve	500				500
Housing & Commercial Growth Fund	700				700
Commercial Income Protection Reserve	758		13		771
Playgrounds Reserve	109	(30)	69		148
Decriminalisation Reserve	141	(141)			--
Enterprise Reserve	1,177	(560)	619		1,236
Climate Change Reserve	498	(122)			376
<b>Sub-total - Specific Earmarked Reserves</b>	<b>10,998</b>	<b>(4,646)</b>	<b>1,407</b>	<b>--</b>	<b>7,759</b>
Revenue Grants not yet applied	1,468	(509)	19		978
<b>Total - All Earmarked Reserves</b>	<b>12,466</b>	<b>(5,155)</b>	<b>1,426</b>	<b>--</b>	<b>8,737</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 at this time.

#### 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. Without proactive action to deliver the Balancing the Budget initiatives, the council could find itself in a position where it has limited capacity to respond to and manage the impact of any significant or unexpected events or emergencies during 2024-25 and set a budget for 2025-26.
- 4.2. 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 in line with but not exceeding the referendum threshold set in place by the Secretary of State, resulting in a Band D council tax increase of £6.57 relating to the Gravesham Borough Council element of the charge in 2024-25.

- 4.3. 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 £3.73m in 2026-27, requiring base budget reductions beyond those contained within the budget setting report.
- 4.4. 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.