South Oxfordshire District Council

Report of the chief financial officer on the robustness of the budget estimates and the adequacy of the reserves.

1. Section 25 of the Local Government Act 2003 places a duty on the chief finance officer (at this council the interim head of finance) to make a report to the council on the robustness of the estimates and the adequacy of the reserves. This report fulfils this requirement and provides councillors with assurance that the budgets have been compiled appropriately and that the level of reserves is adequate. It is a statutory requirement that councillors must consider this report when considering and approving a budget.

2. In presenting this report the interim head of finance is mindful of other associated statutory safeguards designed to prevent the authority from over-committing itself financially, namely:

    - Section 151 of the Local Government Act 1972 which requires the authority to make arrangements for the proper administration of its financial affairs and that the interim head of finance as chief finance officer has personal responsibility for such administration;
    - Section 32, 43 & 93 of the Local Government Finance Act 1992 which requires the authority to set a balanced budget;
    - The Prudential Code introduced as part of the Local Government Act 2003 sets out the framework within which the authority must manage its investments, including adequate planning and budget estimates;
    - The external auditor's duty to assess the adequacy of the authority's proper arrangements to secure economy, efficiency and effectiveness ('value for money').

3. To reinforce these obligations, section 114 of the Local Government Finance Act 1988 requires the interim head of finance as chief finance officer to report to all the authority's councillors, in consultation with the monitoring officer and chief executive, if there is or is likely to be unlawful expenditure or an unbalanced budget.

Robustness of the budget estimates

PREPARATION, REVIEW & SCRUTINY

4. In accordance with best practice and using accruals accounting, the council provides for realistic estimates of costs and known liabilities.

5. The initial budget estimates were prepared jointly by the heads of service and appropriately qualified staff from the council's finance team. These have been reviewed and challenged by the council's strategic management team and cabinet members.

6. The 2021/22 budget briefing session held with members on 9 February 2021 provided an explanation of the factors taken into account in determining the budget.

REVENUE BUDGET

7. Similar to most district councils the most significant costs within the revenue budget are:

    - staff salaries and related costs
    - payments under contracts for services
    - housing benefit and council tax support payments.

8. The estimates of staff costs are prepared by calculating the cost of employing each member of staff for the full year. The budget also includes the costs of recruiting to posts that are currently vacant, unless it has been decided that the post will not be filled. The costs include incremental progression and an allowance for the cost of any locally agreed pay award.

9. Under normal circumstances, the risk of overspending on staff costs is considered negligible. The risk of under-spending on staff costs is high, so I have assumed a level of expected vacancy savings and this year, the council has budgeted at 96 per cent of the expected salary level in its services. However, due to the ongoing Coronavirus pandemic, the council's contingency budget for 2021/22 has been significantly increased, which could be used to support additional staffing costs to support the council's ongoing response.

10. The costs of the most significant council contracts are linked to increases in the various price indices, usually the Retail Prices Index (RPI) or the Consumer Price Index (CPI). Allowance has also been made within the budget for additional costs arising from demographic growth and increased demand for services (e.g. additional properties leading to increased waste collection costs).

11. The risk of overspending on contract costs exists and there remains a financial risk from a contractor failing to deliver services in accordance with the contract. Such risks are managed through the council's contract monitoring and risk management procedures, but cannot be eliminated.

12. The cost of housing benefit is largely met through government subsidy. However, because of the large sums involved, there is a significant financial risk to the council of fluctuations in subsidy income and income from housing benefit overpayments. This risk is outside the council's control. The level of local authority errors in the latest grant subsidy claim is safely below the government's threshold. The risk of any cost falling on the council is therefore low and continues to be mitigated by close contract management. The anticipated income from housing benefit overpayments has also been reduced in this year's budget.

13. The areas of expenditure where there is a greater level of risk are within the demand led budgets such as the costs of homelessness (including temporary accommodation). Experience of demand in the current and recent years has been used to inform the 2021/22 budget. Again, additional contingency budget has been provided for 2021/22 to support the council's response to the Coronavirus pandemic.

14. A number of revenue income streams are sensitive to changes in market conditions and therefore there will always be a risk that budget targets are not met.

These include planning fees, building control fees, and land charges fees which all respond directly to the fluctuating characteristics of the housing market. Car parking income can also be volatile and responds to the general economy and retail market. Previous budget-setting exercises have made adjustments to reflect prevailing market conditions. As a result of the pandemic, and the even greater uncertainty that this creates, a significant provision for income losses has been built into the 2021/22 budget.

INVESTMENT INCOME

15. The returns on the council investment portfolio are relied upon to support the cost of services. The continuing impact of low interest rates has been factored in to the MTFP reported as part of the budget setting report.

16. Investments are diversified in accordance with the treasury management strategy, and the earnings assumptions in the budget are set prudently. Investment income is not committed until the year after it is earned. There is therefore certainty about the amount available when the budgets are set.

REVENUE CONTINGENCY SUM

17. The council has for some years now included a revenue contingency sum of £200,000. As noted above, due to the pandemic, additional contingency budget had been built into this budget of £900,000, together with a provision for income losses of £925,000.

FUNDING FROM CENTRAL GOVERNMENT

18. Whilst government funding for 2021/22 has been outlined in the provisional local government finance settlement, this is a one-year settlement only. Future government funding remains uncertain due to delays in progressing:

    - The fair funding review
    - the review of the business rates retention scheme
    - the review of New Homes Bonus

19. Government grant funding has been projected to decline over the medium-term financial plan period. The projections could be too optimistic or too pessimistic. If they are too pessimistic then the council’s reserves are considered adequate to compensate until future budgets can be reviewed.

CAPITAL PROGRAMME

20. The council’s project management system is used to manage capital schemes. This is designed to reduce the risks of both underspends and slippage in the programme.

21. The capital programme is split into an approved programme and a provisional programme. This split is made to give greater certainty of costs and timescales before a final commitment is made. This requires a detailed appraisal to be agreed by the relevant cabinet member before expenditure is committed.

22. For major projects the council engages skilled advisors to assist it. Whilst these measures can manage and mitigate risks, by their nature some capital schemes will still contain significant financial risks.

23. In the capital programme recommended to the cabinet, allowance has been made for works considered necessary to the council's land and property assets.

24. The council has sufficient capital contingency and reserves to meet any potential capital overspends. While the use of these reserves would reduce the interest income earned, the impact would not be significant. The investment income is not committed until it has been earned.

MEDIUM TERM FINANCIAL PLAN

25. An updated MTFP has been included in the budget report. The plan sets out provisional revenue spending plans and the estimated use of reserves through to 2025/26.

26. Using balanced but prudent estimates of future government funding shows that the council should be able to set a balanced budget throughout the MTFP period. However, the increasing annual draw on reserves over the MTFP period is unsustainable over the longer term and, unchecked, will mean it will not be able to continue to set a balanced budget in future years.

27. The transformation activity, which was identified in last year's budget setting report and now forms part of the corporate plan delivery activity, is central to the council's efforts to tackle the increasing budget gap. It will take place against the backdrop of the new corporate plan priorities. Those priorities may themselves have to be reviewed to help ensure that the council's finances become more sustainable in the future.

PRUDENTIAL INDICATORS

28. The prudential code requires the calculation of a number of prudential indicators, which measure the sustainability of the council's MTFP, explicitly with regard to affordability, prudence, value for money, stewardship, service objectives and practicality. This is backed up by a specific requirement to monitor performance against forward-looking indicators and report and act on significant deviations.

BUDGET MONITORING

29. At the end of May, August and November heads of service complete budget monitoring returns forecasting their year-end positions which are reported to Cabinet.

RISK MANAGEMENT & INSURANCE

30. The risk management arrangements are managed by the council's risk and insurance officer.

31. The main risks inherent in the council's MTFP are:

    - government grant funding is less than estimated;

    - long-term economic impact of the Coronavirus pandemic;

- Unforeseen growth in essential expenditure.

Adequacy of reserves

32. The Chartered Institute of Public Finance and Accountancy (CIPFA) has issued guidance on local authority reserves and balances in Local Authority Accounting Panel (LAAP) bulletin 55. It sets out the three main purposes for which reserves can be held:

    - A working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – which forms part of general reserves;

    - A contingency to cushion the impact of unexpected events or emergencies – also part of general reserves;

    - A means of building up funds often referred to as earmarked reserves, to meet known or predicted liabilities.

33. The council's Medium Term Financial Strategy (MTFS) states that the council will hold £50 million of investments of which £35 million can be invested in capital schemes that will produce a return of certainty. The remaining £15 million can be invested in treasury investments. Such principles may need to be reviewed and potentially adjusted in accordance with the future level of government funding.

34. Whilst the treasury investments are capable of being realised, investment in capital schemes is not capable of being realised. By the end of the MTFP period it is projected that at least £30 million of the £35 million permitted to be invested in capital schemes will have been invested or earmarked for investment.

35. Excluding the £50 million investment, the council is projected to hold £10.9 million of general revenue balances and £7.0 million earmarked revenue reserves as at 31 March 2026.

Conclusion

36. The budget estimates have been prepared following a properly controlled and professionally supported process. They have been subject to challenge and due consideration, and the identifiable risks should be capable of management.

37. Overall, the level of reserves is adequate in relation to the proposed revenue budget and capital programme, both for 2021/22 and over the medium-term period to 2025/26. However, the council's MTFP shows that it faces a significant budget challenge over the next five years and beyond as it increasingly draws more from its reserves to support a revenue budget that is already in deficit. The scale of the challenge of ensuring that reserves continue to be adequate will be determined in large part by how generous or not the government's future funding schemes prove to be for our council.

Simon Hewings (Interim head of finance and chief finance officer)

8 February 2021