APPENDIX K

REPORT TO	ON
Full Council	24 February 2021

TITLE	REPORT OF
Report of the Chief Finance Officer	Deputy Director of Finance (s151)

Is this report confidential?	No

PURPOSE OF REPORT

1. To provide advice to the Council as required under s25 of the Local Government Act 2003.

RECOMMENDATION

2. The Council are recommended to note the Chief Finance Officer's comments and advice under Section 25 of the Local Government Act 2003 as set out in this report and have regard to it when considering the budget proposals for 2021/22.

REASONS FOR RECOMMENDATION

3. This comments of the Chief Finance Officer are required by statute as the Chief Finance Officer should report to members the robustness of the budget estimated including how they have been constructed and the assumptions that underpin them. In addition, the Chief Finance Officer must report to members the adequacy of the proposed financial reserves.

OTHER OPTIONS CONSIDERED AND REJECTED

4. The comments within this report are a statutory requirement and as such no other options are considered

EXECUTIVE SUMMARY OF REPORT

5. This report outlines the key assumptions and risks contained in the budget and identifies that over time working balances will be increased to mitigate some of those risks.

6. Budget assumptions have been made based on the Provisional Local Government Finance Settlement that was announced on 17 December 2020. The Government has announced that the budget will be published on the 3 March 2021. South Ribble Council will revert to membership of the Lancashire Business Rates Pool. In addition, the

Government maintained New Homes Bonus allocations in 2021/22 however it will remove New Homes Bonus allocations by 2023/24.

7. The Government has supported the economy through the Covid-19 pandemic through various grants and other initiatives. Grants of over £36m have been made available to South Ribble Council to enable it to support council services, its communities and local businesses. This investment in public services is welcomed, however Government borrowing is estimated by the Office for Budget Responsibility (OBR) to reach £393.5bn by the end of 2020/21 compared to £58bn in 2019/20. This level of public sector debt will necessarily require the Government to bring future public finances to a more sustainable position. It is possible therefore that future Government investment in public services will be curtailed.

8. It is my view that the outcome of the fair funding review, expected for 2022/23, will result in the Government reducing funding for district councils and possibly transferring some of this to upper tier authorities, many of which will continue to struggle to fund adult social care and children's services. The uncertainty created by the new business rates regime means we must be prudent when budgeting for future levels of retained business rates, as such I have assumed that the benefit of pool membership in 2021/22 will not continue in 2022/23 onwards.

9. In terms of the 2021/22 budget once again all key budgets have been reworked to align with expected outturn for 2020/21 and therefore reflect the ongoing cost of delivering the current levels of service.

10. The forecast is that the budget will be balanced in 2021/22 and that the Council's **general fund balances** will be over £4.0m. The general fund balance is above that of other Lancashire District Councils and is required to manage short-term one-off risks to the revenue budget. Funds continue to be set aside as earmarked reserves in 2019/20 that will:

    - support the delivery of the council's corporate strategy
    - enable the council to support its residents and businesses during the Covid-19 pandemic.
    - help mitigate some of the risks within the current and proposed new business rates system.

11. Key risks remain, in particular the forecasting of **business rate receipts** in 2022/23 onwards. The council will benefit from being a member of the Lancashire Business Rate Pool in 2021/22. However, the new 2022/23 75% retention scheme is unlikely to resemble the current pool scheme. As such the benefit in 2021/22 will be treated as a one-off and only growth that is achieved in the business rates base will be built into the base budget. It is prudent to assume zero percent growth over the medium-term period.

12. The council continues to develop its **Capital Strategy**, this report demonstrates that the council's capital expenditure and investment decisions are taken in line with corporate objectives and take account of stewardship, value for money, prudence, sustainability and affordability. I am satisfied the report, Appendix H to the main budget report, provides this assurance to members and outlines what the strategic intent is for the council over the medium to long-term.

13. Having reviewed the underlying assumptions and commented on the position in relation to key risks and working balances I am satisfied that the budget assumptions are reasonable, the key financial risks have been considered and the budget is deliverable.

14. Further analysis of the risks to revenue and capital budgets are analysed at the end of this report.

CORPORATE OUTCOMES

15. The report relates to the following corporate priorities: *(tick all those applicable):*

An exemplary council	✓	Thriving communities	
A fair local economy that works for everyone		Good homes, green spaces, healthy places	

BACKGROUND

16. Under the requirements of Section 25 of the Local Government Act 2003 the Chief Finance Officer is required to advise members when setting the budget as to the robustness of the estimates and the adequacy of working balances.

THE ROBUSTNESS OF ESTIMATES

17. In terms of the budget proposals, once again in 2020/21 a thorough reassessment of the budgets has been undertaken by budget holders, service managers and directors and their accountants based upon the latest information available. In terms of the key assumptions contained particularly in the 2021/22 budget these are shown in the main budget report but are summarised for convenience below

KEY ASSUMPTIONS

18. The table below shows the key assumptions made in forecasting forward the Council's financial position. Further analysis is provided in Appendix F – General Fund Forecast Assumptions.

Key Assumptions	2021/22	2022/23	2023/24
Growth in Council Tax Base	0.40%	0.50%	0.50%
Council Tax Increases	0.00%	0.00%	0.00%
Increase in Retained Business Rates through Growth	0.11%	0.00%	0.00%
Total Forecast New Homes Bonus	£363k	£93k	£0
Future Service Pension Rate	16.4%	16.4%	16.4%
Pension Fund Deficit Recovery	£72k	£75k	£75k
Additional Business Rates - Lancashire Pool 21/22 Transitional Business Rates Income 22/23	£1.638m	£0.807m	£0.000m
Pay Award	0%	2%	2%

In terms of the key assumptions I would make the following comments to confirm their validity:-

COUNCIL TAX INCREASES

19. The administration is proposing no increase in council tax in 2021/22. The MTFS does model future increases however it is acknowledged that this will be revisited every year and will depend upon the outcome of the business rates and fair funding review. A prudent 0.5% expansion of the council tax base, excluding council tax increases, is being assumed which is in line with growth experienced in previous years.

REDUCTION IN RETAINED BUSINESS RATES

20. The council will benefit from being a member of the Lancashire Business Rates Retention Pool in 2021/22. However, the 75% business rates regime, expected in 2022/23, is unlikely to resemble the pool and therefore the council may experience a reduction in retained business rates in the medium term, for example:
    - the final scheme may change the tier splits and provide more of the retained rates to upper tier authorities
    - when the new system is reset the Government may reduce or remove the section 31 grants, these are grants that compensate councils for Government initiatives that reduce locally generated business rates e.g. small business rates relief or retail reliefs. These grants currently equate to £1.465m a year and therefore any reduction in these grants poses a large risk to the council.
    - the quantum of business rates in the system may include the New Homes Bonus allocations that the government is phasing out over the next three years.

21. The new business rates regime will dictate the quantum of business rates to be shared nationally and locally however it is the fair funding review that will dictate how this is shared out. The fair funding review is expected to generate new funding 'baselines' for all councils in 2022/23. How these will be calculated, and therefore how much the council will be allocated, is still not finalised however it is believed it will be based on factors such as population growth, rurality, deprivation levels and other local area adjustments such as local labour costs. The fair funding review will allocate retained business rates based on a council's relative need to all other councils, as a result of this it is not possible for the council to conduct any meaningful analysis of the likely outcome of this review. At this stage South Ribble Council will assume the benefit of pool membership, approximately £1.6m, will be permanently lost by 2023/24 as a result of the business rates and fair funding review. The budget assumes a transitional year in 2022/23 whereby 50% reduction is experienced.

22. The budget report explains the volatile nature of this particular core income stream and why accurate forecasting of future receipts is problematic. The income levels contained within the retained business rates budget are based upon a set of assumptions that may impact on the total amount collected in future years, in particular the outcomes within the appeals process. The council has set aside over £3m in reserves to manage one-off fluctuations in retained business rates.

23. A final consideration to the council's retained business rates income is the potential for there to be a national economic slow-down. This is further discussed in Appendix F – General Fund Forecast Assumptions. In brief this may result in an increase in the

number of appeals against rateable values as well as reducing local economic activity and therefore reducing retained business rates. The council's share of provision for appeals will stand at £3.290m in 2021/22, an increase of £0.600m, which is comparable to the national average.

NEW HOMES BONUS

24. The spending review announced a gradual reduction and ultimate removal of New Homes Bonus. Government proposals are for allocations to reduce as follows:
    - 2021/22 – 3 year allocation - for South Ribble Council approximately £363k
    - 2022/23 – 1 year allocation - for South Ribble Council approximately £93k

25. The following announcement was made with the finance settlement in 2021/22:

    The government has committed £622 million to continue the New Homes Bonus scheme in 2021-22. The scheme financially rewards councils for the number of additional new homes they built, locally incentivising housing growth and creating homes for local residents. We will soon be inviting views on how we can reform the scheme from 2022-23 to ensure it is focussed where homes are needed most.

26. As such there may be a replacement to New Homes Bonus however nothing can or has been assumed in the budget.

LOWER TIER SERVICES GRANT

27. The Government calculates every year the council's core spending power that is a combination of the council's council tax income, business rates income and new homes bonus grant allocation. For 2021/22 the reduction in new homes bonus is not offset by the assumed additional income that the council would receive if it chose to increase council tax charges by 2%. As such the government has introduced a one-off £100k grant to compensate the council in 2021/22 called the Lower Tier Services Grant. This is an un-ringfenced grant that has been included in the council's funding streams.

BORROWING

28. The council took £10m of temporary (3 month) borrowing in 2020//21 to ensure the council managed its cash balances at the beginning of the pandemic. The council also secured a temporary £6m overdraft. Since then the council has managed its cash balances without the need for further borrowing. The assumption built into the 2021/22 forecast is that the internal cash balances will be sufficient to manage the cash flow requirements of the council, even as the council begins investing in large scale capital projects such as Worden Hall and affordable housing.

29. The treasury implemented a 1% increase in PWLB borrowing in 2020/21 however this increase has been reversed for 2021/22 and with it is brought a number of reforms. The largest change is that the council will no longer be able to borrow from PWLB if it has <u>any</u> investment in its capital programme for purely commercial reasons. This is not a risk to the council's current capital programme as all investments have other non-commercial objectives. However, moving forward, this will prohibit the council from investing anywhere in its capital programme purely for investment returns.

30. The council's 2021/22 budget includes an income budget of £200k for income earnt on its cash balances. The current base interest rate is at an historic low of 0.1%. With the continuing expiry of investments placed at higher, pre-pandemic, interest rates and their replacement at significantly lower returns, it may not be possible to maintain the same level of performance during 2021/22.

31. The budget for interest earned has been reduced from £300k in 2020/21 to £200k in 2021/22 to account for this however the budget will be reviewed and, if required, adjusted in 2021/22 to account for continued low interest earnt.

PENSION FUND CONTRIBUTIONS

32. As part of a triennial pension review the Lancashire County Pension Fund announced an increase in employer pension contributions for 2020/21 to 2022/23 to meet the future costs of the scheme. The contributions have increased from 14.4% to 16.4% resulting in an increase in the council's contribution. The same contribution rate is assumed for 2023/24 although this will be reviewed when the new three-year review is undertaken.

PAY AWARD

33. The Government spending review announced a pay freeze in 2021/22 for the majority of public sector staff with a guaranteed a pay rise of at least £250 for all staff that earn less than £24,000 per year. These assumptions have been included in the pay budget for South Ribble Council in 2021/22 although these Government proposals are not yet agreed with public sector unions.

34. The spending review also announced that national living wage will rise from £8.72 to £8.91 an hour and will be extended to workers aged 23 and over from April 2021 This will not affect South Ribble Council's pay bands for 2021/22 as the council pays above this level already.

35. Looking further forward, the budget includes a 2% pay increase for all staff in 2022/23 and 2023/24. This assumption adds approximately £200k to the pay budget each financial year.

MEDIUM TERM FINANCIAL STRATEGY

36. The MTFS sets out the Council's plans to bridge the funding gap as summarised below:

Balancing the Budget

	2021/22 £m	2022/23 £m	2023/24 £m
Cumulative Budget Deficit/(Available Resources)	**0.150**	**1.905**	**3.290**
Shared Services	(0.288)	(0.288)	(0.288)
Shared Services – Additional	(0.040)	(0.120)	(0.120)
Shared Services – Phase 2 Forecast	0.000	(0.100)	(0.100)
Staff Turnover	(0.150)	(0.150)	(0.150)
Parking Income	(0.018)	(0.018)	(0.018)
Adjusted Budget Deficit/(Available Resources)	**(0.346)**	**1.229**	**2.614**
Contribution to Leisure Services Deficit	0.346	0.000	0.000
Forecast Council Tax Increase – 0% 21/22, 1.99% 22/23 & 23/24	0.000	(0.162)	(0.324)
Future Transformation Savings/Additional Income	0.000	(1.067)	(2.290)
Net Budget Deficit/(Available Resources)	**0.000**	**0.000**	**0.000**

37. The level of future savings required to balance the budget will be largely dependent upon the outcome of the Fair Funding Review and Business Rates Review as well as the recovery of leisure services. Both the impact of this review and the date of implementation remain unknown but are forecast to reduce the council's funding by £1.6m by 2023/24

38. The strategy shows that broadly speaking the administration will attempt to bridge the gap by generating efficiency savings and additional income.

39. The greatest budget challenge for the council is to generate £2.1m of efficiency savings by 2023/24. Significant savings have already been identified from the first phase of **shared services** and both councils are successfully expanding these arrangements. A **programme of service reviews**, working with services to identify service savings and efficiencies.

40. The council is bringing forward a number of developments that will produce **additional income** sources in the medium term. Revenue models for these schemes will be developed in 2021/22 including for the Affordable Housing and Extra Care schemes. In addition, a review will be undertaken of the council's existing commercial portfolio to ensure that it delivers the most effective returns.

41. I am satisfied that these efficiency saving targets, although challenging, would be achievable if the council were to experience such a reduction in business rates income.

LEVELS OF RESERVES

42. The level of general fund reserves is over forecast to be approximately £4.0m over the medium term. This is higher than general fund balances at most Lancashire District councils and importantly the MTFS does not rely on utilising balances to meet deficits over the three-year period. General fund balances are there to manage potential risks contained in the budget particularly around:
    - the volatility in the funding system in relation to business rate retention
    - possible re-profiling of savings and income generation proposals into future years
    - risk of loss of deposits should a future banking crisis occur

43. There are risks to revenue budgets surrounding the major capital projects that may begin to generate income towards the end of the medium-term strategy. These include the risk of voids in the council's affordable housing stock. In addition to this, there continues to be uncertainty surrounding the effects of the United Kingdom's withdrawal from the EU and the recovery of the national economy post-Covid. Further analysis is provided in Appendix F to this report.

44. To manage this uncertainty the council will create a Covid Recovery Fund of up to £500k to support local businesses and communities. In addition, the council has created a £150k earmarked reserves to help manage one-off reductions in income at its investment sites.

45. I deem the general balances of £4m and the earmarked reserves prudent given the risks facing the council and its residents and businesses.

IMPLICATIONS OF REPORT

46. This report has implications in the following areas and the relevant Directors' comments are included:

Finance	✓	Customer Services	
Human Resources		Equality and Diversity	
Legal	✓	Integrated Impact Assessment required?	
No significant implications in this area		Policy and Communications	

EQUALITY AND DIVERSITY

47. None

AIR QUALITY IMPLICATIONS

48. None

COMMENTS OF THE STATUTORY FINANCE OFFICER

49. These are contained within the report.

COMMENTS OF THE MONITORING OFFICER

50. The report is designed to ensure that the relevant legislation is complied with in terms of Statutory Officer advice.

James Thomson
Deputy Director of Finance (s151)

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RISKS TO MEDIUM TERM FINANCIAL STRATEGY

The Medium-Term Financial Strategy outlines how the Council will achieve its corporate strategy priorities whilst recognising the budgetary pressures it will experience over the coming 3 years. Within the strategy are a number of risks that are outlined below.

RISKS TO REVENUE BUDGET

HIGH RISK

75% Business Rates Retention
The government continues its ambition to implement a new 75% business rates retention scheme for all local authorities by 2022/23. The council will continue with the Lancashire Business Rates Pool in 2021/22. Forecasting the effects of the new retained scheme using prior year data is challenging for the following reasons:

- The local preceptors should receive more of the locally generated business rates (from 50% to 75%) however, the government may introduce a less favourable split between lower and upper tier authorities
- The level of locally generated business rates may be reduced if the government reduces its allocations of section 31 grants – grants used to compensate councils for Government policies that reduce business rates e.g. small businesses and retail reliefs
- The current pool uses historic baseline funding levels however, the result of the government's fair funding review will see this baseline adjusted with the potential for South Ribble Council to receive less of its retained NDR income.

The government continues to develop the fair funding review and new business rates system however it remains uncertain when the new system will be introduced. There remains a lot of work to be completed by the Government including the need to develop transitional arrangements. After this a consultation exercise will need to be undertaken. The budget is prudent and assumes implementation of the fair funding review and 75% business rates regime in April 2022 however this is far from certain.

Post-Covid Recovery
The pandemic has impacted on the council finances as well as the wider economic environment. This has created more uncertainty in the early stages of the MTFS. To mitigate this risk the Government has provided £1.481m (20/21) and £0.505m (21/22) of unringfenced funding. The council will also receive compensation for loss of some fees and charges for April to June 2021 and is also able to spread any council tax or business rates deficits in 2020/21 over the next three years (as opposed to the usual one year).

To help manage this uncertainty the council will create a Covid Recovery Fund of up to £500k to support local businesses and communities. The council has also created a £150k earmarked reserves to help manage one-off reductions in income at its investment sites.

The MTFS has in place some funds to help the council manage the Covid recovery period however the full medium-term impact of this recovery is not yet clearly understood. This could yet impact further on council expenditure, income and Government funding levels.

MEDIUM RISKS

Business Rates Appeals and Other Business Rates Adjustments
The Council's shareprovision for business rates appeals stood at £2.69m at the beginning of 2020/21 and allowance has been made for additional provision of £0.6m during the year. Of this, during the year there has been approximately £24k of successful backdated appeals charged to the provision.

In April 2017 a new business rates appeal process was introduced called 'Check, Challenge and Appeal'. The benefit of the multi-stage process is that it requires businesses to complete its own 'Check' and therefore should discourage speculative appeals. To date there has been no successfully challenged appeal reported by the VoA against the 2017 list. The VoA has focussed on clearing the backlog of prior year appeals and so it is prudent to assume more appeals will be coming through from the 2017 list in 2020/21.

Recently a number of press reports stated that the VOA had agreed a 25% rebate in office rates, worth around £481m nationwide, due to the impact of the pandemic. The argument for the rebate is that due Covid the office sector have experienced lower demand, realise lower rental values and as a result have lower rateable values. No agreement has been made with the VOA however it is understood it is in discussions that cover a number of property types. The council has 536 offices with rateable value of £8.5m. This highlights the potential volatility of the business rates system and is why the council must be prudent when setting aside reserves and provisions to manage this income stream.

The budget for 2021/22 includes further additional provision of £0.6m. This is deemed sufficient to meet the potential successful appeals that may transpire from the outstanding lists.

Pay Inflation
The Government has proposed a pay freeze for Council staff in 2021/22, except for those on lower pay, and this has been assumed in the budget. Negotiations with the employee unions is not complete and so it is possible a higher pay settlement may be approved. Every 1% increase in pay results in over £100k of additional expenditure to South Ribble Council. An average 2% pay increase per year has been assumed for 2022/23 to 2023/24.

Universal Credit
The Government is consolidating a number of welfare benefits into a revised Universal Credit Scheme. One of these is housing benefit which is currently administered by the Council. Universal credit will be managed by the Department of Work and Pensions. The full scheme was rolled out in South Ribble in July 2018 however take up has been slow. There is the potential risk that bad debts will increase when people move to UC as it becomes more difficult to recover overpayments. This is because the housing benefit element of debt might not have the same priority over other debt recover such as fuel or rent arrears. We have seen an increase more over the last 12 months from HB to UC as take-up has increased and therefore, there is a possibility that the council's bad debt provision will need to be increased with a subsequent charge to the general fund.

Delivery of Budgeted Savings and Additional Income

The MTFS includes potential cumulative savings targets of £0.9m and £2.1m in 2022/23 and 2023/24 respectively. Achieving these goals will require a change in organisational culture, enhanced sharing of services across organisations and further capital investment in income generating schemes. The monitoring and robust challenge of all proposals is overseen by the council's Shared Services Management Team. Risks are reported to Shared Services Management Team. as well as members and actions taken when required. Given the council's likely increased dependency on generating income there will always be some risks that sit outside of the council's control and are therefore more difficult to manage.

The council's general fund balance of £4m has been set such that potential delays in bringing forward income or generating savings can be temporarily managed within council resources.

As noted in the report the council is still able to borrow from PWLB at low rates to fund its capital programme. However, Government reforms have meant that in order to utilise these funds the council is prohibited from investing anywhere in its capital programme purely for investment returns. Although this will not affect the council's current capital programme, it will reduce the scope of investments the council can pursue in order to generate income and therefore balance future revenue budgets.

Existing Income

The major income streams the council benefits from include planning, garden waste subscriptions and trade waste collection as well as commercial income from investment properties the council owns. Uncontrollable reductions in income could leave services under-funded. The council has been prudent when budgeting for income and has set aside an income equalisation reserve of £150k for its investment properties to manager any temporary voids from these units.

Interest Rates

The council's 2021/22 budget includes an income budget of £280k for income earnt on its cash balances. The current base interest rate is at an historic low of 0.1%. With the continuing expiry of investments placed at higher, pre-pandemic, interest rates and their replacement at significantly lower returns, it may not be possible to maintain the same level of performance during 2021/22.

LOW RISK

Inflation

The council's expenditure is subject to annual inflation based on indexation that is determined by external stakeholders. Sharp increases in inflation would result in higher day to day expenditure and possible budget overspends. Inflation forecasts from the Office of Budget Responsibility (OBR) have been used to inform the budget over the coming 3 years. The OBR forecasts inflation to remain below the Bank's 2% target rate until at least 2025. Inflation is only applied to specific council contracts including the waste collection contract. This will be reviewed annually to ensure budgets are sufficient to meet inflationary pressures however it is expected that inflation will remain low throughout the MTFS period.

RISKS TO CAPITAL BUDGET

MEDIUM RISKS

Overspends on Capital Projects

All capital projects are monitored on a monthly basis, with the major capital projects monitored on an ongoing basis by council officers and commissioned external project managers. Any potential overspends are highlighted by the relevant project group or officer and reported to the Chief Finance Officer.

Actions plans are agreed to manage potential overspends and managed by the project officer. If necessary, financing is identified within the capital programme to meet any additional required resources. Changes to the capital programme are reported quarterly to Executive Cabinet. Changes to a capital project between these periods are taken on a separate report to Executive Cabinet or Full Council.

LOW RISK

Insufficient Financing to Delivery Capital Programme

The council continues to have a significant gap between its capital funding requirement and current borrowing levels. As such borrowing is available to the council if funding sources previously allocated to projects no longer become available.

Insolvency of Major Contractor

As part of the tender process the financial standing of each contractor has been thoroughly assessed. These checks are regularly and the council's subscription to a credit check agency provides alerts were the credit status to change.