Chief Finance Officer Statement on the Budget Robustness

1 Background

1.1 The Local Government Act 2003 places a statutory duty on the Chief Financial Officer (CFO) to review the Medium Term Financial Strategy and comment upon the robustness of the budget and the adequacy of the reserves to be held by the authority when it is making the statutory calculations required to determine its Council Tax or precept. The authority is required to take this report into account when making that decision.

1.2 Section 26 of the Local Government Act 2003, places an onus on the CFO to ensure the authority 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.

2 Report of the Chief Financial Officer on the robustness of the 2018/19 budget proposal.

2.1 It is the opinion of the CFO that the draft budget for 2018/19 is based upon a sound financial strategy that will enable the Council to deliver its proposed Council Plan successfully.

2.2 Both the Revenue Budget and Capital Programme have been formulated having regard to a number of factors including funding availability; risks and uncertainties; inflation; priorities; demography and service pressures. The savings plans have been formulated having regard to Council priorities and assessed against an agreed set of impact criteria and equality assessments. As the budget and Government funding is becoming increasingly complex, especially with the increasing importance of partnerships, risk management is key to the setting of budgets and reserve levels.

2.3 As the development of the Council Plan and budget for 2018/19 has progressed, the position has been subject to reviews with Chief Officers, other officers and Members, including Cabinet and Scrutiny Committees. Due consideration has also been given to reconciling the over-arching financial strategy with corporate priorities and hence all the proposals have been developed as an integral part of service planning (the process known as Reconciling Policy, Performance and Resources).

2.4 The 2018/19 budget is balanced and, in finalising the draft budget, consideration has been given to unforeseen issues that could arise during the year and ensuring that those risks can be managed. The strategic risk register has been reviewed and an analysis of ESCC's financial position in the current year has been carried out, to identify direct impacts and risks that are inherent within the 2018/19 budget. Notwithstanding that the draft budget for 2018/19 is balanced, there are significant risks to the budget, arising from the requirement to realise £17.051m of revenue savings. The County Council holds a general contingency of £3.5m (an increase of £0.060m on 2017/18) to cushion the impact of unexpected events and emergencies in year (within the base revenue budget). Additionally there is a sum for agreed potential additional borrowing, the capital programme risk provision, of £11.2m.

2.5 Increasing the Council Tax will provide a more sustainable and increased income to the Council which will help to protect services. Implementing the Adult Social Care precept will support and help protect services that are already under significant pressure.

3 The Adequacy of Reserves

3.1 Reserves are a key element of the Council's financial management arrangements. Reserves can be broadly categorised as follows:

- A working balance to manage in-year risks, called the General Fund Balance;
- A means of building up funds to meet known or predicted requirements, called General/Earmarked Reserves.

General Balances

3.2 For the General Fund Balance there are two main approaches taken by Councils to determine their required minimum level; either by a straight percentage of the Council's current spending: or an assessment of risks and the impact they will have on the Council's overall financial position.

3.3 In 2016/17 an exercise was carried out using data drawn from a range of national benchmarking and comparison sources to determine the percentage, a number of Local Authorities have historically used 5% of net revenue spending as a sound base for determining the minimum level of reserves. This would equate to £18.6m for 2018/19.

3.4 A risk-based assessment of issues, which could have a major impact on the Council's finances, provides a more flexible and responsive approach that better reflects the continuously changing environment within which Local Government has to work. This approach will take into account the type of risk, the potential magnitude of the financial risk and a judgement as to how likely the issue is to arise. Table 1 below identifies a number of the high level risks that may have financial implications, which assist in determining the required minimum level of General Fund Balance to be retained.

Table 1: 2018/19 Risks

Risk	**Potential magnitude**	**Estimate of potential impact**	**Magnitude £m**
Growing demand for services is already impacting on service budgets particularly in Children's Services (CSD) and Adult Social Care (ASC). Service departments are forecasting a £2.4m overspend.	ASC 2018/19 budget £166.5m. CSD SEND budget for 2018/19 £7.9m.	2% increased unfunded demand	3.5
Unforeseen activity which impacts directly on departmental budgets over and above the £3.5m within the general contingency.	Net Service Budget £371.3m	1% increased unfunded demand	3.7
Risk that inflation on utilities and other areas where budgets were not uplifted for inflation become unmanageable within budget allocations.	Total utilities and other budget 2018/19 circa £69m.	2% increase in current provision.	1.4
Many of the proposed savings are complex with delivery plans still to be finalised. Therefore a risk exists that it will not be possible to make the planned savings within the timeframe required.	Total planned savings in 2018/19 are £17.1m.	10% non-achievement	1.7
Non achievement of Fees & Charges targets built into the revenue budget, due to the continuing economic climate.	Planned Fees & Charges for 2018/19 is £61.6m	Underachievement provision of 5%	3.1
Business Rate Revaluation significantly increases risk of inaccurate forecasts.	Reduction in anticipated revenue from Business rates local share of £11.6m.	Rates collected reduces by 5%	0.6
Changes in historic weather patterns may be being the potential for adverse weather conditions which may present the Council with additional unfunded costs. The impact of weather as opposed to additional prevention cannot be quantified.	Historic winter maintenance spend is circa £1.1m.	10% increase in costs due to adverse weather	0.1

3.5 Taking everything into account, the General Fund Balances of £10.0m, is sufficient based on professional judgement which, given the level of risks, is a minimum general balance and remains lower proportionately than a lot of other authorities. This is considered adequate on the basis that the budget balances for 2018/19 and that, in addition, as noted at 2.4, an in-year contingency is held.

Reserves

3.6 The Council's approach to the management and accounting for earmarked reserves is set out in the Reserve Strategy adopted by the Cabinet in June 2017. The Reserves have been reviewed using the principles set out in the Policy ensuring that they are reflective of the Council's strategic agenda and the current financial risks and issues the Council faces through the medium term.

3.7 It is crucial to bear in mind that the reserves are the only source of financing to which ESCC has access to fund risks and one-off pressures over a number of years. If ESCC minimises the level of reserves too significantly there is a risk that in future, the ability to properly manage these emerging costs will be significantly hampered. Reserves can only be spent once and the possibility of creating new reserves in an era where budgets are tight and can become overspent, not just individually but corporately, is increasingly limited.

3.8 The reserves are split into two categories: named service reserves and strategic reserves, as set out in the Reserve Policy. ESCC reserves are estimated to total £88.6m as at 1/4/18. The actual Reserves at 1/4/17 totalled £103.5m;

Table 2 Summary of Earmarked Reserve estimated at 1/4/18

	£m
Held on behalf of other or statutorily ringfenced	*19.9*
Waste Reserve	12.8
Set aside for the new Capital Programme 2018/23	21.0
Insurance	5.5
Strategic Reserves	
Risk Reserve	3.1
Priority Outcomes and Transformation Reserve	7.8
Financing Reserve	18.5
Total ESCC service specific reserves	**68.7**
Total Reserves	**88.6**

Planned use of ESCC specific reserves is estimated to reduce them to £30.3m by the end of the MTFP period in 2020/21.

3.9 The **named service reserves** comprise:

- **Held on behalf of other or statutorily ringfenced** of £19.9m – most significantly this comprises £10.5m schools balances and ring fenced public health reserve of £4.4m, which cannot legally be spent on ESCC activities.
- **Waste Reserve** – the Waste reserve is £12.8m. Financial risks relating to the waste contract are reviewed and managed through this reserve on a 4 year rolling programme;
- **Set aside for the Capital Programme 2018/23 –** The updated Capital Programme (presented at Appendix 7) runs to 2023. The current investment required for basic need (essential budgets, such as schools places and highways infrastructure) and the remaining 2013/18 programme, of £444.2m has been identified. The remaining £21.0m reserve was agreed to support this programme and to reduce the need to borrow and therefore the revenue pressure on the current MTFP and beyond; and
- **Insurance** – the reserve of £5.5m is based on an actuarial review of insurance liabilities that have arisen over previous years, and represents the liability that the actuary estimates will become payable in 2018/19 and beyond. It is proposed that the £0.4m reduction in requirement from 2017/18 will top up the transformation and priority outcomes reserve together with the reduction in provision of £0.3m.

3.10 The estimated brought forward balance of **the 3 strategic reserves** was £31.6m as reported at state of the county (SoC), this has been increased for the £5.8m agreed to be set aside at SoC to manage identified risks to the MTFP including the unachievement of savings and business rate income and the estimated gross underspend of £1.0m reported at Q2. With agreed calls of £9.0m reducing it to £29.4m. These are itemised below:

- £18.5m Financing Reserve – This is held to manage known issues with a one-off or short-term financial impact or one off remedial action while resolutions are sought over the life of the MTFP. Its brought forward balance was £17.8m at SoC. The main changes have been, additional set aside of £6.8m as noted above at 3.10 and use of £6.1m; mainly for MTFP smoothing (agreed as part of the 2016/17 budget), cost of redundancies and the election in May 2017. Estimated planned use over the MTFP period reduces this to £4.1m.
- £7.8m Priority Outcomes and Transformation Reserve – To fund the specified initiatives to change, protect and improve Council services, with particular emphasis on:
    - Invest-to-save
    - Seed funding for innovation (notably digital) and developments contributing to the County Council's priorities.
    - Investment in the redesign of the way that services are delivered

  Its brought forward balance was £5.2m at SoC. The main changes have been an increase from insurance provision and reserve of £0.7m and a net increase of £1.9m following the realignment of the risk reserve less planned use in year. Estimated planned use over the life of the MTFP reduces this to £3.4m.
- £3.1m Risk Reserve – To fund actions that mitigate the potential financial consequences of risks recognised in the Council's Corporate Risk Register and the CFO's robustness statement. Its brought forward balance was £8.6m at SoC, £5.8m of its planned use being transferred to the priority outcomes and transformation reserve to reflect changes in the reserves policy and an additional £0.3m from insurance claims and £1.4m for increased taxbase and collection fund.

3.11 There are a number of significant areas of change that currently are not fully understood and cannot be fully quantified but will have potential financial impact over the planning period, these include:-

- Changes to the Local Government finance system to pave the way for the implementation of Business Rate Retention. As part of these reforms, the main Local Government grant will be phased out and additional responsibilities devolved to Local Authorities. This will be through incorporating existing grants including Public Health (effectively ending the ring fence) and Revenue Support Grant. The new responsibilities are as yet unknown and could bring significant risks to funding, particularly if they are demand led. Business Rate Retention will sit alongside the implementation of the outcome from the fair funding review, and the Government have announced they will aim for local authorities to retain 75% of business rates from 2020/21. Business rates will then be redistributed according to the outcome of this new needs assessment. It is not currently possible to estimate the impact of this on the Council until further detail is provided; and
- The Fair Funding Review consultation and outcome. Which will be the basis of the new needs assessment upon which the business rates will be redistributed.

The uncertainty regarding the future finance system means it is increasingly important to hold sufficient reserves to manage this unquantifiable financial risk. Therefore every opportunity should be taken to top up the Council's strategic reserves.