REPORT TO:	**FINANCE and MANAGEMENT COMMITTEE**	**AGENDA ITEM: 11**
DATE OF MEETING:	**24 FEBRUARY 2021**	**CATEGORY: RECOMMENDED**
REPORT FROM:	**STRATEGIC DIRECTOR (CORPORATE RESOURCES)**	**OPEN**
MEMBERS' CONTACT POINT:	**KEVIN STACKHOUSE (01283 595811)** **Kevin.stackhouse@southderbyshire.gov.uk**	**DOC:** u/ks/budgets/budget 2021 22/Section 25 Report 2021Final Council
SUBJECT:	**ANNUAL REPORT OF THE SECTION 151 OFFICER**	
WARD(S) AFFECTED:	**ALL**	**TERMS OF REFERENCE: FM 08**

1.0 Recommendations

1.1 That the Annual Report of the Section 151 Officer is considered and noted.

1.2 That the Council has due regard to the Annual Report when approving the Budget for 2021/22 and when considering future proposals for new spending and the utilisation of resources.

1.3 That no new spending commitments are added to the Base Budget and Medium-Term Financial Plan approved by the Finance and Management Committee on 11 February 2021, pending the outcome of the Government's Fair Funding Review.

1.4 That the Medium-Term Financial Plan is reviewed and updated following details emerging from the Government's Fair Funding Review which is expected in autumn 2021.

2.0 Purpose of the Report

2.1 In their role as the Council's Section 151 (Chief Finance) Officer, the Strategic Director (Corporate Resources) is required, under Section 25 of the Local Government Act 2003, to provide an overall opinion on the robustness of the estimates included in budgets and the adequacy of Council reserves.

2.2 In doing so, the Report also includes an assessment of the Council's financial sustainability based on its spending plans and projected resources available, as set out in its Medium-Term Financial Plan (MTFP).

2.3 It is recommended that Elected Members of the Council pay due regard to the Annual Report when approving the Budget for 2021/22 and when considering proposals for new spending and the utilisation of resources.

3.0 Executive Summary

Overall Opinion of the Section 151 Officer

3.1 Based on the Budgets submitted for approval and the latest MTFP, the Council's current financial position continues to look healthy ahead of 2021/22.

3.2 However, over the planning period to 2025/26, the position could deteriorate based on current spending, together with projections regarding funding, with the MTFP highlighting the General Fund falling below its minimum balance of £1.5m by 2025/26. Significant budget deficits are forecast after 2021/22 which will reduce the current General Fund Reserve from approximately £11.6 million in 2021 to £1.27 million by 2026.

3.3 On the positive side, projected spending allows for growth associated with residential development and other provisional expenditure such as additional waste collection costs, vehicle and IT replacements, etc. The MTFP also continues to assume that current service provision is maintained over the planning period, with allowances for inflation on pay and contracts, etc.

3.4 Although the Council can control its expenditure base and has time to take corrective action in a timely and planned manner if necessary, it cannot as easily control its external funding and in particular that provided by Government which accounts for approximately 60% of the Council's funding (the remaining 40% is met from Council Tax).

3.5 The biggest uncertainty and consequently the main risk to the Financial Plan, is Government funding from April 2022. As previously reported, this will depend on the final outcome and details of the Government's Fair Funding Review, including any changes to the redistribution of Business Rates and the replacement for the New Homes Bonus.

3.6 During 2020/21, the Council's "Financial Resilience Index" (*compiled by the Chartered Institute of Public Finance and Accountancy*) compared to other shire districts broadly confirmed the Council's position.

3.7 This Index highlighted that the Council's current level of Reserves places the Council at a lower risk of financial difficulties with its sustainability measure being high in comparison to many other authorities. Indeed, the Council's position appears to have strengthened compared to other authorities from that reported in 2019/20.

3.8 However, the updated Index for 2020/21, also highlighted that the Council continues to be at a higher risk when it comes to the reliance on Government funding.

3.9 An additional and independent study, commissioned by the Society of District Treasurers in 2020, highlighted the Council's strong position compared to other district councils. This study also highlighted the Council's resilience and ability to better recover from the effects of Covid-19, compared to many other authorities.

3.10 As reported during 2020/21, the Council has incurred additional costs and a reduction in income due to Covid-19. However, Government funding received to-date should, based on current estimates, compensate the Council without any longer-term effect on the MTFP; this is being kept under review.

3.11 Although the Council remains in a positive Financial position, it should guard against complacency and continue to operate with a certain degree of caution. Where-ever possible, opportunities to generate efficiency and budget savings should be pursued with the concept of providing Value for Money being at the core of all Council spending.

3.12 The Section 151 Officer is aware that there may be proposals to meet certain spending pressures, which are not included in the MTFP. Re-directing current resources and/or using earmarked reserves should be considered where there may be greater pressure to spend.

3.13 In the meantime, until the Council's future funding position is more certain, it is recommended that no further financial commitments, beyond the proposed Budget and MTFP recommended by the Finance and Management Committee on 11 February 2024, should be made.

4.0 Detail

Basis of the Opinion

4.1 The Opinion is given within the general context detailed below, followed by a summary of each of the Council's main accounts and their financing. Reference is made to the separate budget reports considered by the various Policy Committees during January and February 2021.

4.2 The opinion also considers a broad independent analysis of the Council's financial resilience.

General Context

4.3 It is considered that estimates of income and expenditure included in the Base Budget and longer-term financial forecasts are prudent. They provide for inflation and other known variations (pensions, pay awards, etc.) together with provisions that recognise current cost pressures, Corporate Plan priorities and potential costs associated with Growth of the District.

4.4 The Budget for 2021/22 and forward projections are based on the most up-to-date economic forecasts for inflation and interest rates, etc. The Budget does not assume a vacancy rate for staffing and prudently assumes that all posts on the Council's Establishment are filled throughout the year.

4.5 In addition, a realistic but prudent view has been taken regarding projected income levels from fees, charges and short-term investments. This also includes a prudent reduction in Government funding in the form of Retained Business Rates and the New Homes Bonus (or its replacement) pending the outcome of the Government's Funding review.

4.6 Forward projections for Council Tax receipts are based on an increase in property numbers which are less that those contained in the Local Plan. Given the impact of Covid-19, they have also been scaled back for 2021/22 and 2022/23 compared to previous forecasts.

4.7 The compilation of detailed budgets has been undertaken in conjunction with service/budget managers and reviewed by the Council's senior management.

4.8 It is recognised that the Council has well established performance and budget monitoring arrangements in place to help ensure that Council finances are monitored effectively. This includes quarterly reports to the Finance and Management Committee, in addition to statutory reports regarding the Annual Accounts and the Annual Budget.

4.9 The Council has traditionally spent within budget and generated additional income over that estimated. Although this is no guarantee of future performance, it does provide some comfort that budget preparation and budget management is sound.

4.10 The Council's Financial Strategy directs the Council to plan its spending over a 5-year rolling period for the General Fund and 10 years for the Housing Revenue Account (HRA). This provides an indication of the sustainability of spending plans and the projected level of Reserves. Consequently, this allows sufficient time in which remedial action can be implemented to address any issues in a planned and timely manner.

4.11 A full risk assessment, with mitigating actions, is considered alongside the MTFP for both the General Fund and the HRA.

Financial Resilience

4.12 The Chartered Institute of Public Finance and Accountancy (CIPFA) published a Financial Resilience Index in December 2019. This was updated in January 2021. The Index sets out the Council's position on a range of measures associated with financial risk, with a comparison to similar authorities.

4.13 The Index was based on 8 measures, although they can be distilled down to 3 categories to illustrate the Council's position as shown below.

Financial Stress Indicator	Comparison Rating
Level and Sustainability of Reserves	Lower Risk
Debt level and interest payable	Higher Risk
Financing	Higher Risk

Reserves

4.14 The Council's current level of Reserves highlights that the Council is in a much stronger position compared to many other shire districts.

Debt Level and Interest

4.15 The Council does have a high level of debt associated with the HRA which it inherited from the Government under the "self-financing system" in 2012/13. It is considered that the comparison with other authorities is influenced by the fact that many shire districts do not have their own housing stock, with over 50% of all authorities having transferred their stock to a Registered Social Landlord/Housing Association. There is a risk that this could skew the comparison.

4.16 Nevertheless, the level of outstanding debt for a district council is large at £58m. However, the cost of the debt and its repayment remains affordable within the HRA's Financial Plan and the financial model for the HRA is designed to ensure sums are set-aside on an annual basis to repay the debt. £30m is due to be repaid over the life of the current Financial Plan.

Financing

4.17 The Council is placed at a higher risk due to its reliance on the Government's funding system. Although the Council does not receive any Revenue Support Grant, its level of income from Business Rates, due to Growth, is considerably above its Baseline Level set by the Government in the current funding system.

4.18 Therefore, the Council is at risk to changes in the funding system and in particular if/when the Baseline Level is reset. If the Council's need is assessed as far less than that currently due to its Growth, then the Council could be penalised through an increase in its Levy.

4.19 This would be exacerbated if the Council were not part of the Derbyshire Business Rates Pool as no Levy (50%) is paid on Growth above the Baseline.

*(**Note**: The Levy is effectively the amount that the Council pays to the Government from its 40% share of local Business Rates as part of the redistribution system of local authority resources)*

4.20 The Index also highlighted that the Council does not generate as much income from fees and charges compared to other authorities. Again, this comparison may be influenced by the fact that the Council does not charge for car parking and will be in a minority of authorities who don't charge.

4.21 Perversely however, this has had a positive impact on the Council compared to other authorities during Covid-19 as income losses have not been as acute and impacted on the financial position.

Vulnerability and Recovery Index

4.22 In August 2020, the Society of District Council Treasurers commissioned Grant Thornton UK LLP to undertake analysis and the development of a Covid-19 Vulnerability and Recovery Index for all districts in England.

4.23 This was to understand the potential impact of Covid-19 on district councils, together with the vulnerabilities which need to be considered in any recovery plans. This formed part of a submission to Government regarding the allocation of future resources and to highlight the pressures specific to district councils.

(***Note**: The published report was contained in the Council Agenda on 5 November 2020 for information but was not fully considered at that time due to the on-going pandemic*)

4.24 Six key indicators made up the Index, including one specifically relating to the financial vulnerability of each authority. The Council was ranked as one of the top three (least vulnerable) in England regarding financial vulnerability, i.e. its financial position shows itself to be strong and more likely to be resilient to the pressures of Covid-19, compared to other district councils.

General Fund Revenue Account

4.25 The Base Budget for 2021/22 highlights a budget deficit as previously forecast, which will be financed from the General Fund Reserve, as planned.

4.26 Increasing budget deficits are forecast in the next four years of the MTFP, potentially becoming significant by 2025/26. This is based on current expenditure increasing and current funding decreasing and is perhaps a worst-case scenario.

4.27 As highlighted above, this is mainly due to the uncertainty regarding Government funding beyond 2021/22.

4.28 As a Growth area, the Council should continue to benefit from any system based on the delivery of new housing and business. However, this will depend on Government priorities and how much funding is awarded to shire districts for distribution.

4.29 As the Resilience Index highlights, the Council is at risk form changes in the current funding system and the current uncertainty makes future planning more difficult. The MTFP prudently assumes that overall funding will fall towards its baseline funding assessment and if this is the outcome for the Council, potential deficits will need to be addressed early in the planning period.

4.30 Growth also brings additional demand on the Council's services and it is noted that the MTFP continues to set-aside (as yet unallocated) sums in the Base Budget to meet future costs.

General Fund Reserve

4.31 The current level of the Reserve continues to remain healthy. The projected level of the Reserve over the medium-term planning period is summarised below.

2020/21	£11.6 million
2021/22	£10.8 million
2022/23	£9.2 million
2023/24	£6.9 million
2024/25	£4.3 million
2025/26	£1.2 million

4.32 The above table shows that the General Fund Reserve is projected to reduce quite significantly over the current planning period. This allows the financing of committed capital projects and asset replacements, together with budget deficits, which include provisions to increase spending arising from Growth.

4.33 Under statute, the Council has to maintain an unallocated contingency in its General Reserve. The Council has set a minimum level of £1.5 million (around 10% of net expenditure) to be maintained. As the above table highlights, the Reserve could fall below that figure by 2025/26 based on current projections.

4.34 The Budget Report considered by the Finance and Management Committee on 11 February highlighted more significant deficits projected from 2022/23. Therefore, the position will need to be kept under review in order that the Council does not become over reliant on reserves, unless they are replenished.

Housing Revenue Account (HRA)

4.35 The HRA also remains in a healthy position and the current 10-year Financial Plan shows a sustainable position. It is noted that the Plan is based on a rent increase of 1% for 2021/22 and CPI + 1% from 2022/23. The HRA General Reserve is currently forecast to remain at or above the minimum contingency level of £1 million over the life of the planning period.

4.36 Resources have been set-aside to deliver a capital programme of works and to maintain services at their current levels.

4.37 Although the HRA Plan currently appears sustainable, the Social Housing White Paper is likely to increase the need for additional capital works to ensure enhanced safety in all dwellings, for example, carbon monoxide monitoring and higher levels of electrical safety. The capital programme includes budgets for works of this nature although potentially not at the level required.

4.38 The Council is also expected to deliver improvements to dwellings to reduce the carbon footprint. This aim is contained within the Council's Corporate Plan, but the costs associated with improvements of this type have not been factored into the Financial Plan and could be significant. Grant funded is expected to be available to assist but may not cover the costs in full.

4.39 Resources have also been set-aside to repay debt. It is noted that the financial model for the HRA is designed to generate sufficient surpluses to maintain the original debt repayment schedule approved in 2012/13 as highlighted earlier in the Report.

4.40 The HRA's risk analysis shows that the main issues potentially are the continuing level of Right to Buys, future Government policy on Rents beyond 2023/24 and the external financing of the Supporting People Programme.

4.41 Complete loss of funding for Supporting People will result in a £1.3m reduction in income across the 10-year Plan. An added risk with Supporting People is the aging software. An upgrade will be required to transfer the service from analogue to digital which potentially will result in one-off costs of up to £0.5m. This is not included within the Financial Plan at this stage.

4.42 However, given the current position of the HRA, any remedial action required can be achieved in a planned and timely manner, although a more detailed review of resources may be required if the risks impact as highlighted above.

Capital Expenditure and Financing

4.43 All capital projects both in the General Fund and the HRA, have sufficient resources set-aside to finance the associated expenditure.

4.44 The Council still has access to a level of uncommitted General Fund receipts, and it is expected that potential asset sales over the MTFP period, will generate further resources. This will be driven from the Council's Asset Management Plan and Economic Development Strategy.

4.45 Overall, there are no major concerns currently associated with capital expenditure and it's financing.

Treasury Management

4.46 The General Fund is currently debt free. Council expenditure is not reliant on any borrowing and given the current level of reserves and cash on deposit, it is unlikely that the Council will need to enter into any form of borrowing over the financial planning period.

4.47 The HRA debt is mainly at fixed interest rates and provision is being made in the HRA's financial plan to repay loans in accordance with a repayment schedule. A proportion of variable rate debt is currently costing significantly less than that budgeted so this provides some contingency should interest rates increase. This loan is due to be repaid in March 2022.

4.48 The Council is not reliant on interest rates increasing to generate a return on investments. A prudent assessment has been made in the MTFP for interest and dividends on investments and this is below the amount actually being generated. An increase in rates would be beneficial for the MTFP.

4.49 The Treasury Management Strategy includes a Lending Policy and Counterparty List. This is designed to ensure the liquidity and security of investments, rather than yield, although during Covid, this has come under some pressure as interest remain near to, or even below zero,

4.50 Besides the level of interest rates and the risk of negative rates becoming the norm, there are no other concerns associated with the Council's current treasury management position.

Other Usable and Earmarked Reserves

4.51 The Council maintains various reserves that are used to meet one-off/known commitments or to defray expenditure over a number of years, for example, ICT upgrades, vehicle replacements and community development projects.

4.52 Reserves held to finance on-going community and sports development spending, will need to be kept under careful review if external and partnership contributions significantly reduce. On-going contributions to asset replacement reserves are provided for in the MTFP.

4.53 Overall, it is considered that current reserves will remain sufficient to meet commitments over the life of the current MTFP. In addition, they should continue to be reviewed on an on-going basis to determine whether they are still required or can be reassigned to meet emerging cost pressures.

5.0 Financial Implications

5.1 None as a direct result of this report.

6.0 Corporate Implications

Employment Implications

6.1 None.

Legal Implications

6.2 None.

Corporate Plan Implications

6.3 None. The production of the Section 25 Report is a statutory requirement.

Risk Impact

6.4 None.

7.0 Community Impact

Consultation

7.1 None required.

Equality and Diversity Impact

7.2 None.

Social Value Impact

7.3 Not applicable.

Environmental Sustainability

7.4 Not applicable.

8.0 Background Papers

8.1 None