# ANNEX 2

## ROBUSTNESS OF THE BUDGET

CONTENTS

**Robustness of the Budget and Adequacy of Reserves**

## 1. Introduction

The Local Government Act (Part II) 2003 requires a council's Chief Finance Officer (CFO) to report to councillors on the robustness of budget estimates and the adequacy of that council's financial reserves. The City Council's CFO (also known as the Section 151 officer) holds the post of Strategic Director of Finance. A summary of this evaluation is set out below.

## 2. Overall Robustness of the Budget

The City Council's annual budget is constructed in order to deliver the Council Plan. However due to the current Covid-19 pandemic the financial planning context has shifted considerably. The Medium Term Financial Strategy (MTFS) is the overarching framework within which the Council's financial planning and management activity takes place. Given the impact of Covid-19 it is necessary to update the MTFS. The annual budget is an integral part of the rolling multi-year Medium Term Financial Plan (MTFP). This approach enables it to support delivery of the Council's priorities and services. It provides the means by which planned spending may be controlled within available resources. Due to the financial impact of Covid-19 it has been necessary to identify in-year savings of **£12.505m** and identify reserves to ensure the viability of the Council's budget position. Therefore, this assessment of the robustness of the budget focuses on the likelihood that actual spending will vary from the interim budget and the subsequent impact on the financial health of the organisation. It will also illustrate the impact on reserves of the current budget strategy and the planned use of reserves in year.

The Council is a going concern and the budget process is part of a continuous service planning and financial cycle. A wealth of knowledge and understanding of the local and national financial and economic environments is used to make informed assumptions and judgements about future financial planning. This activity seeks to establish a robust budget which is appropriate, realistic and constructed having taken a practical and appropriate assessment of risk. The impact of the current operating context is more difficult to predict, however. This is due to the unprecedented impact that the Covid-19 related lock down has had on the Council's financial planning assumptions. This report sets out the direction and actions required over the coming months to ensure the financial sustainability of the Council from this point forward.

### 2a. Financial Environment and Framework

The external framework in which the Council operates continues to be significantly challenging. There have been well documented and growing examples of Public Sector bodies experiencing financial difficulties and this is expected to continue into 2020/21 and beyond until there is a sustainable long term solution to fund public bodies to an appropriate level. The full consequences of Brexit are unknown and likely to influence the imminent and longer term funding for local government. The following section details key elements that have influenced and been noted in the construction of the MTFP.

With the additional adverse impact of Covid-19 the funding envelope for local government has never been under more pressure. Whilst the government has provided additional funding to address the financial impacts of Covid-19 in Nottingham this compensation is estimated to mitigate **51%** of the actual financial impact.

**Previous Financial Performance**

Over previous financial years as with many other Councils in the previous four years (2016/17, 2017/18, 2018/19 and 2019/20) the Council has been over budget. This has been managed by the use of one off resources.

There continues to be pressures on the 2020/21 budget, due to the combined impact of Covid-19 and specific issues in relation to the Council's wholly owned energy company – Robin Hood Energy. At period 4, there was a reported forecast overspend of **£1.202m**. This overspend position takes into account the impact of Covid-19, Robin Hood Energy, Business as usual variances and additional costs in relation to other Council Companies. In order to manage this position in-year savings of **£12.505m** have been identified, reserves of **£38.718m** have been identified for permanent release and a further **£31.304m** of reserves have been identified to be utilised in year and subsequently paid back.

**Use of one off measures**

During the last 4 years, there has been a consistent use of one off measures and mitigating management actions used in arriving at the final outrun position spends. The range of management actions required have included:

- reducing contingency balances
- reviews of earmarked reserves
- reduced revenue contribution to the capital programme
- vacancy freeze controls
- stop to non-essential spend and reductions to maintenance spend
- restrictions on travel and conferences

The interim 2020/21 budget includes **£12.505m** of in year savings, of these **£10.3m** are one-off items or one-year savings in order to present a balanced position. The continued use of reserves and one off measures have had the impact of deferring the more significant changes that are required to balance the revenue budget to secure future financial sustainability. It should be noted that based upon the most up to date financial position available **49.3%** of the Council's earmarked reserves will be utilised to balance the budget in 2020/21. Whilst this is in line with central government policy which directs Councils to utilise reserves to manage the financial impact of Covid-19 the use of these resources represent a significant shift in the overall financial health of the Council. It needs to be recognised there are significantly diminishing options for the use of one-off measures and the budget flexibility of the Council is now severely limited.

**2018/19 External Audit – key issues and recommendation**

The 2018/19 external audit has not yet been concluded. However, the 2017/18 external Audit report from KPMG details key issues and recommendations in relation to financial sustainability and the use of one off measures.

> *"Sustainable Financial Budget*
> *The Authority has highlighted a number of risks regarding its ability to deliver a self-sufficient and sustainable financial budget in the medium term. Many of these risks are not specific to the Authority but to the sector as a whole, underpinned by reduced central funding and increasing demand for social care services.*
>
> *The Authority's outturn for 2017/18 and 2016/17 has been overspend against budget. For 2017/18 the Authority has relied on a number of non-recurrent measures to help reduce the in-year overspend. Despite setting a balanced budget for 2018/19, it is likely that there will be emerging financial pressures that will require co-ordinated action by CLT."*

**Report in the Public Interest**

In August 2020 the External Auditor issued a Report in the Public Interest regarding the Council's wholly owned energy company Robin Hood Energy (RHE). The report and its recommendations were fully accepted by the Council and considered at a full Council Meeting on the 27th August 2020.

The report made the following recommendations in relation to the MTFS:

> *The Council should ensure that it reflects the financial pressures arising from RHE alongside those from covid-19, demand-led services and other areas to produce balanced and achievable financial plans for the current year and for the medium-term, without disproportionate, unsustainable reliance on one-off measures.*

**Demand led pressures, income generation and reduced flexibility within the budget**

The CIPFA Financial Resilience Index, together with other benchmarking data, shows the Council has a higher financial risk from the high local demands for the Council's Children's and Adult Services. These demand led services account for an increasing percentage of the overall net budget requirement and therefore it reduces the Council's net budget for other areas. This in turn impacts on the Council's ability and flexibility to make future savings, at a time when there are significant gaps in the budget for 2021/22 onwards.

Added to the above is the impact of Covid-19 on the Council to generate income. A significant component of the previous budget strategy was to maximise income via a commercial approach, whether that be from internally provided traded services or external companies in the Council's Group. Covid-19 has had a disproportionate impact on the financial health of the Council due to the reliance upon income as part of the Council's MTFP. Further work is being undertaken to understand the long term impact on the Council's MTFO in relation to income and options are being developed to de-risk the Council's budget in this area.

**CIPFA Financial Resilience Index**

In response to the unprecedented financial challenges faced by local government, CIPFA has developed a Financial Resilience Index to act as an analytical tool for chief finance officers to support good financial management and shows the council's position on a range of measures associated with financial risk. The latest information released in 2019 represents the second year of the index and the areas of high and low risk for Nottingham are consistent with the previous year's assessment. The model shows that Nottingham is carrying risks in the following areas:

- **Council Budget Flexibility** – ratio of total spending on Adults Social Care, Children's Social Care and debt interest to net revenue expenditure. Nottingham has reduced budget flexibility
- **Change in unallocated Reserves** – the average percentage change in unallocated reserves over the past three years. Nottingham has used unallocated reserves more quickly than comparator groups – in subsequent assessments given the significant use of reserves recommended in the Interim Budget report this indicator will worsen in future assessments
- **Unallocated Reserves** – the ratio of unallocated reserves to net revenue expenditure. Nottingham has a low level of reserves in relation to comparators
- **Grants to Expenditure ratio** – the proportion of net revenue expenditure funded by central government grants. Nottingham faces risks if grants are not maintained
- **Council Tax Requirement / Net Revenue Expenditure** – a low Council Tax ratio and therefore a higher dependency on grants may suggest future financial difficulties as grants diminish further. Nottingham has a limited ability to raise revenue from Council Tax when compared to others
- **Children's Social Care ratio** – ratio of spending on Children's Social Care to net revenue expenditure. Nottingham has a higher proportionate spend on Children's services than others in the comparator groups

- **Adults Social Care ratio** - ratio of spending on Adults Social Care to net revenue expenditure. Nottingham has a higher proportionate spend on Adults Social Care services than others in the comparator groups

The following areas are where the Council has been assessed at a lower degree of Financial Stress risk:

- **Earmarked reserves** - the ratio of earmarked reserves excluding Public Health and Schools to net revenue expenditure. Nottingham carries significant earmarked reserves in relation to others (including PFI) – this will change given the recommended use of reserves in the Interim Budget
- **Level of reserves** – the ratio of current level of reserves excluding Public Health and Schools to net revenue expenditure. Nottingham holds a number of earmarked reserves
- **Retained Income from Rate Retention / Net Expenditure** – ratio of retained income from business rates as a proportion of net expenditure. As locally raised business rates becomes an increasing percentage of income a higher ratio is seen has having less financial stress for the Council

The use of reserves to support the 2020/21 interim budget will significantly reduce the Council's earmarked reserves and will therefore adversely impact on the CIPFA Financial Resilience Index.

**Symptoms of financial stress**
In addition to the financial resilience index, CIPFA has also provided guidance to public bodies regarding the signs that an organisation is suffering from financial stress indicators. This is summarised below:

- **Running down reserves or a rapid decline in reserves -** using up reserves to avoid cuts can only provide temporary relief
- **Failure to plan and deliver savings** to ensure the council lives within its resources
- **Shortening medium-term financial planning horizons -** could indicate a lack of strategic thinking and an unwillingness to confront tough decisions
- **Greater "still to be found" gaps in saving plans**
- Growing tendency for **unplanned overspends and/or carrying forward undelivered savings** into the following year - sign an authority is struggling to translate its policy decisions into actions

As can be seen from the results of the resilience index Nottingham is experiencing most of the above such as depletion of reserves and unplanned overspends. In order to mitigate this position a full MTFS and MTFP will be published in December 2020, which will demonstrate how the Council will continue to remain financially stable in the medium term.

**Public Accounts Committee**
In March 2019 the Public Accounts Committee released a paper on Local Authority Financial Resilience. A key theme of the paper was the level of reserves and the unplanned use of the resourced by Local Authorities. The paper references the concerns over the uncertainty of future funding and that debates have been held whether there is sufficient funding to enable Local Authorities to discharge their statutory duties. It also had regard to media reports of financial difficulties of Local Authorities since the crisis of Northamptonshire County Council.

The paper makes it clear that the funding of local government is a key concern across the sector and the outcomes of the nation funding changes will be fundamental in ensuring that Authorities are financially sustainable.

**Medium Term Financial Outlook (MTFO) - Fair Funding Review**

The final settlement has confirmed funding for 2020/21 only, the introduction of the Fair Funding Review and 75% Rates Retention has now been further delayed due to the impact of Covid-19, therefore funding for 2021/22+ is unknown and the MTFO assumes funding for 2020/21 will continue for 2021/22+. No assumptions have been made for the likely impact on future settlement funding due to a lack of clear exemplifications of the Government policy options being currently considered. The exception to this is in relation to additional funding to mitigate the adverse financial impact on the collection fund of Covid-19 and a further **£5m** has been assumed based upon high level information from central government.

**2b. Internal Measures to monitor the financial performance**

Monitoring the financial results and forecasts of the Council in the short and medium term remains a priority and a number of improvements to the process have been implemented as a direct result of the on-going external framework in which the Council operates, these include:

- Weekly risk based assessment of the Council's financial position
- Weekly Corporate Leadership Team meeting dedicated to Financial Management
- Weekly Political Leadership meeting dedicated to Financial Management
- Development of a Transformation Programme Structure to deliver new ways of working
- Enhanced monthly monitoring to CLT
- Budget Manager budget packs
- State of the nation paper – a periodic briefing looking at the authority's overall financial position, including reserve, capital, borrowing levels and financial risk analysis

**Weekly risk based assessment of the Council's financial position**

The Finance Leadership Team meet on a weekly basis to consider the risk position in relation to the Council's finances. The assessment is based upon a number of key indicators and a judgement is made regarding the overall health of the financial position. This risk assessment is then circulated to the Corporate Leadership Team and the Portfolio Holder for Finance.

**Weekly Corporate Leadership Finance Meeting**

The financial risk assessment plus the overarching financial strategy of the Council are considered by the Corporate Leadership Team on a weekly basis.

**Weekly Political Leadership Finance Meeting**

The financial position plus the overarching financial strategy of the Council are considered by the Political Leadership Team on a weekly basis.

**Development of Transformation Programme**

A re-invigorated Transformation Programme is being developed to design new ways of working to deliver a financially sustainable future for the Council. An update regarding progress and plans will be provided in the full MTFS update in December 2020.

**Enhanced monthly monitoring to CLT and Leadership**

The Council's financial controls are set out within financial regulations, allowing significant assurance of the strength of financial management and control throughout the Council. Given the current climate this process has been reviewed with improvements made to give CLT a comprehensive monthly pack. This details the forecasted outturn, variance commentary together with more detailed information by department. Regular updates are also provided to Leadership and Executive with a quarterly report presented to Executive Board.

**Accountability Letters – Annual Budget Manager budget packs**

Budget Managers are accountable for delivering their services within budget and are required to forecast the outturn position at regular intervals within the financial year, typically monthly. To support Budget Managers with this requirement an annual budget pack is issued prior to the start of the new financial year including the detailed pay budgets, together with non-pay budgets and a statement of the new year budget savings or funded pressures. There is a requirement for Budget Managers to sign their Accountability Letters when taking receipt of their budgets for 2020/21.

**New Financial System – Oracle Fusion**
A new Finance system was due to go live in April 2020, however due to the impact of Covid-19 the project has been delayed to April 2021. The Council will be moving to Oracle Fusion, part of this change includes the requirement for new accounting codes. Budget Managers are being supported through this transition by a series of engagement session, training and budget packs.

**State of the nation paper**
At the start of the 2018/19 financial year a report was presented to CLT outlining the 2017/18 outturn, financial outlook and risks and issues for 2018-2022, since the introduction of this paper there have been periodic refreshes of the report. The purpose of this report was to bring together the current financial outlook for the Council and describe the associated financial risks and the resulting impact on the financial sustainability of service delivery. This paper has been updated and refreshed then subsequently been used as part of the 2020/21 budget strategy. The approach will continue to develop in line with the construction of the full MTFS in December 2020.

**Constructing the MTFP**
The environment and framework described above has significantly influenced the construction and governance around of the latest MTFP. Throughout the process there has been effective and extensive engagement by Senior Colleagues, Finance Colleagues and Executive Councillors.

<u>Assumptions</u>
Underlying assumptions have been examined and found to be satisfactory as follows:

- The funding for inflation is considered to be appropriate, being consistent with known trends and reasonable forecasts
- The income aspects of the overall budget are calculated based on previous and current trends, known influences and identified risks – the impact of Covid-19 however presents a significant forecasting challenge and will be kept under constant review.
- There are appropriate bad debt provisions in place, however the impact of Covid-19 represents a significant challenge in determining appropriate levels of bad debt provision and will be kept under constant review
- Other known trends and potential overspends (e.g. demographic changes, new legislation, etc.) have been evaluated, subjected to various peer reviews and professional challenge and adequately provided for.
- The organisational and financial frameworks and processes required in order to operate within the proposed budget are practical and adequately planned
- Capital receipts used in the funding of the capital programme have been based on professional estimates both of timing and value with a specific risk assessment applied to determine likelihood of receipt. However the impact of Covid-19 is challenging to quantify and will be kept under constant review

**Current Financial Position**

General Fund Revenue
Current monitoring indicates that the forecast General Fund outturn for 2020/21 will show an overspend of **£39.529m** prior to new in year savings and release of reserves, the overspends are in the majority due to the net impact of Covid-19 (after Government funding) of **£38.585m**. Management action is in place to address the overspend as outlined in the interim budget report and the Council is committed to delivering an on budget outturn for 2020/21, however at the current time it is believed that after the use of reserves and the impact of management controls a **£1.202m** overspend will be carried into 2021/22 and the 2021/22 MTFP is predicated on this assumption.

HRA Revenue
The City Council is required to periodically review the HRA to ensure that it does not move into deficit. In order to allow for unforeseen expenditure or loss of income, a working balance is needed. The 2020/21 budget increased the working balance from **£4.000m** in 2017/18 to **£7.727m.** This will provide additional support to mitigate potential financial impact of Universal Credit on the HRA and provide additional one-off funding to cover the early years impact on the new build and acquisition programme. The impact of Covid-19 on the HRA remains challenging to forecast and will be kept under constant review.

## 3. Capital Programme Risk Management & Governance

Capital programme schemes often span a number of years, so it is essential that a longer term view is taken on programming and resourcing.

Capital Programme – Current Position
- General Fund - The forecast spend, including schemes in development, is **£352.413m** and is balanced. The resources to fund the capital programme includes **£18.903m** of capital receipts, of which **£14.333m** are unsecured. A full review of surplus assets is currently being undertaken as part of the disposal and reinvestment strategy and an asset rationalisation board has been established with a focus on realising capital receipts going forward.
- Plans are in place to realise receipts to support the capital programme, however this needs to be kept under review given the emerging picture regarding the economic impact of Covid-19
- Public Sector Housing - The forecast spend to 2024/25 is **£301.806m**

Capital Programme Risk
The proposed five-year programme is ambitious and will require the Council to use a high proportion of available resources. Substantial investment of this nature will result in the Council being exposed to additional risks as follows:

- a significant increase in the authority’s borrowing over the next five years
- the impact of Covid-19 on original capital business cases – in particular the Broadmarsh Shopping centre and Car Park projects
- the impact of Brexit / Covid-19 on construction costs
- the ability to generate capital receipts to fund the programme
- major schemes have a long pay-back period, which will require the use of reserves in the early years to fund short term deficits in business plans
- the cost of feasibility studies are all undertaken at risk
- schemes may not cover their costs or make the desired return.

In order to manage these risks the following key principles will be adopted in managing the capital programme:

- Where new projects are added to the programme that will not cover their costs, an existing project will be removed or amended
- all projects must have a robust and viable business case, which considers and includes whole life costing and revenue implications (including rate of return)
- all schemes will be subject to robust and deliverable business plans and models which demonstrate the necessary return on investment required
- all future schemes will need to address the consequences of cash flow shortfalls in the early years, and available funding must be identified and approved prior to the commencement of projects
- the decision to progress schemes will be dependent on securing the stated level of external funding or grant as appropriate
- new projects will be considered where the Council can make a return on investment;
- where new sources of external funding/grants become available, the programme will be revisited
- all schemes will be subject to an independent internal 'Gateway Review Process'

The Medium-Term Financial Strategy includes the following requirements for consideration of the funding of the capital programme:

- The Council will endeavour to maximise grant funding for schemes which will assist in the delivery of the corporate priorities, part/full grant funded bids will be subject to the same prioritisation process
- Prudential or Unsupported Borrowing can be used where it can be demonstrated that it is affordable and sustainable in the medium term. Borrowing must be within approved limits and in accordance with the prevailing guidance in the Treasury Management Strategy and compliant with the Prudential Code
- Capital Receipts generated from the sale of land, buildings and other assets will be a non-earmarked, council–wide resource, to be allocated according to Council priorities only after a thorough and objective options appraisal and consideration of opportunity costs, and not earmarked to a particular project, scheme, service, directorate and/or geographical area.

The City Council recognises the importance of individual and collective accountability and requires managers to formally acknowledge their responsibilities. Financial management is an integral aspect of effective leadership and good management, relevant Councillors and Officers are required to participate fully in all aspects of capital investment plans.

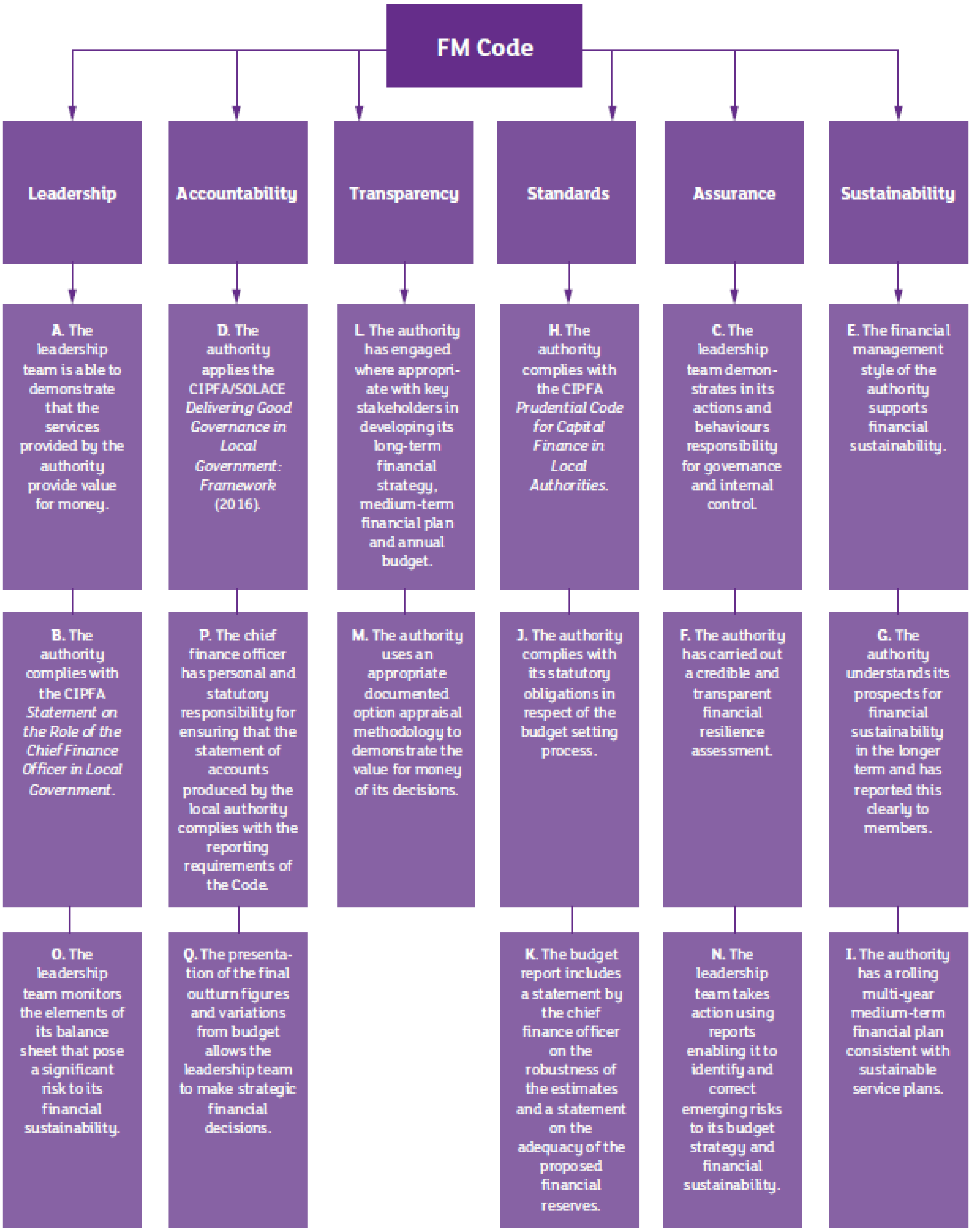
Corporate Directors are accountable for the success and deliverability of all capital projects within their remit; including:
- Ownership of business cases, any subsequent changes to them and the underlying assumptions they are based upon.
- Ensuring that capital projects are delivered in line with agreed targets and resources.
- The successful outcome and benefits realisation of capital projects.

**CIPFA Financial Management Code**

The Chartered Institute of Public Finance and Accountancy (CIPFA) published a Financial Management Code in October 2019. This code is designed to support good practice in financial management and to assist local authorities in demonstrating their financial sustainability. The Code has been introduced because the exceptional financial circumstances faced by local authorities have revealed concerns about fundamental weaknesses in financial management, particularly in relation to organisations that may be unable to maintain services in the future.

The Code applies a principle-based approach and these principles together with the CIPFA Financial Management Standards are illustrated in **Diagram 1** below

**Diagram 1: CIPFA Financial Management Code Principles and Financial Management**



**Standards**

Throughout the Code there are several references that demonstrating compliance is the collective responsibility of elected members, the chief finance officer (CFO) and their professional colleagues in the leadership team.

Local authorities are required to apply the requirements of the Code with effect from 1 April 2020 and CIPFA considers that the implementation date of April 2020 should indicate the commencement of a shadow year and that by 31 March 2021, local authorities should be able to demonstrate that they are working towards full implementation of the Code. The first full year of compliance will therefore be 2021/22. The council will continue to assess its compliance with the new Code at each stage in the 2020/21 financial cycle using the diagram above as a reference point and take the necessary steps to demonstrate sustainability and resilience and ensure its readiness for full compliance in all areas from 2021/22.

## 4. Adequacy of Reserves and Risk Assessment

National decisions regarding public funding and expenditure have been taken by central government to support their stated intention to reduce the national deficit. 2019/20 was the last year of a four-year settlement which confirmed continued reduction in funding in the medium term. This resulted in a significant reduction in the level of funding available to the City Council. Although this has been met with a robust and detailed approach to the identification and delivery of the savings required consequently, the level of cost reduction over the past three years has resulted in a heightened degree of risk associated with delivery of services within budget. The final settlement for 2020/21 was confirmed funding for one year only and the introduction of the Fair Funding Review has been delayed. Funding for 2021/22+ is therefore uncertain.

Whilst the current proposed budget fairly represents sufficient resourcing for current planned activity, this risk cannot be ignored, coupled with the proposed use of reserves set out in the Interim Budget this means that the overall financial position of the Council will need to be addressed with medium term savings plans in the MTFS in December 2020.

The assessment of reserves is even more important in the context of the sustained cuts in funding and the proposed use of reserves in year. It is important to acknowledge that reserves are ‘one off’ funds and are therefore suitable for funding ‘one off’ or unexpected costs. The use of reserves to fund ongoing expenditure is not advised, except in emergencies and/or to enable transition to new ways of working. Given the expectation of central government regarding local authorities to utilise reserves to offset the financial implications of the current pandemic in order to balance the budget in year the use of reserves is appropriate.

Taken together, reserves, contingencies and the processes within the financial framework provide capacity to deal with the changes arising from external forces. This will include, for example: increased demand for services from citizens, changes in legislation and guidance from central government, economic changes, interest rate changes, national emergency incidents and employee relations. This list is indicative rather than exhaustive. The localisation of both Business Rates and Council Tax Support increases the significance of Council reserve levels as these are significant variables on both income and expenditure.

In recommending an adequate level of reserves, the CFO considers and monitors the opportunity costs of maintaining particular levels of reserves. This opportunity cost may be the lost opportunity of investing those funds in service improvement and/or spending on alternative activities. There is a balance to be struck between setting prudent levels of contingencies and reserves considered to be an adequate ‘safety net’ to ensure the Council can operate successfully in a very challenging environment and ensuring sufficient funds are in place for service provision and other Council activities. The levels recommended here are considered to have achieved that balance. This assessment is made on the basis that the MTFP in December 2020 delivers a comprehensive set of savings proposals which demonstrate a plan to ensure that the Council can achieve financial sustainability in the medium term.

**Table 1** shows the estimated Net Revenue Expenditure (NRE) and Unallocated Reserves for Nottingham compared with other Core Cities. The data is taken from the most recent CIPFA financial resilience index and derives from 2018/19 RO returns, demonstrating Nottingham’s reserve position is lower relative to similar councils.

**TABLE 1 : COMPARISION OF RESERVES WITH CORE CITIES**

| Authority | Net Revenue Expenditure £m | Estimated unallocated financial reserves level at 31 March £m | Estimated Unallocated Reserves as % of NRE |
|---|---|---|---|
| Birmingham | 848.785 | 144.050 | 16.97% |
| Bristol | 347.068 | 23.258 | 6.70% |
| Leeds | 517.471 | 27.991 | 5.41% |
| Manchester | 453.377 | 22.045 | 4.86% |
| Newcastle | 230.056 | 10.135 | 4.29% |
| Liverpool | 455.292 | 16.311 | 3.58% |
| **Nottingham** | **240.887** | **7.962 *** | **3.31%** |
| Sheffield | 370.752 | 8.130 | 2.19% |

*£7.962m as reported within the RO returns and represents the opening general fund balance of £9.643m less the 2018/19 overspend of £1.681m

This decision is supported by a comprehensive risk assessment to ensure that the level of reserves represents an appropriately robust financial safety net for the organisation. In assessing these risks the CFO has consulted with relevant colleagues and stakeholders to ensure all risks have been identified. The importance of this work, its depth and accuracy, is further enhanced as a number of the proposals included within the budget plans involve significant changes to ways of working, systems and processes, they involve higher levels of risk than those which broadly maintain current arrangements. At the most practical level those risks begin with the possibility of slippage and disruption in the transition from old to new arrangements. The CFO has sought to ensure that issues of this type and their potential budgetary implications are appreciated by relevant colleagues and Portfolio Holders.

In the event of a second lockdown, if the demands upon the Council are similar to those experienced in the first it will be challenging for the Council to deliver services to the same level and standard. There will not be a sufficient level of reserve to facilitate this, without further additional financial support from central government.

Given the level of savings and the proposed use of reserves included in this Interim Budget the CFO has undertaken an assessment of their deliverability and set out clearly the implications and contingency plans which apply where savings are not delivered as planned. Robust and timely monitoring of savings delivery plans with ongoing contingency planning will be critically important throughout the year.

General Fund

The MTFS requires the opening balance on the general fund to be between 2% and 4% of the total net general fund revenue budget. Following a sustained period of using one off measures to reduce the overspends and to balance the budget the range as defined within the MTFS of between 2% and 4% is deemed inadequate due to the reduced level of budget flexibility, in 2020/21 a review is required to update the MTFS with what the future range for the general fund balance.

The general fund balance has been informed by the detailed risk assessment undertaken as part of the budget process. This requirement will be reviewed during 2020/21 and adjusted accordingly based on any significant change to the risk profile. The opening general fund balance for 2020/21 is **£11.643m**, this represents a **£1.000m** increase from 2019/20 in light of the additional risks and an increase of **£1.000m** pa for the duration of the MTFP. The **£11.643m** excludes the 2019/20 overspend of **£6.754m** because the interim budget includes this prior year overspend, **£11.643m** is **4%** of the general fund budget this together with contingency balance is deemed appropriate.

The level of un-earmarked reserves is expected to be sufficient. However there are the most unusual and serious combination of possible events which if occurred would exceed the un-earmarked reserves and require further action. The most pressing issue in relation to this is the impact of a local lock down or further national restrictions in response to the continuing Covid-19 situation.

The MTFS provides for a central contingency value of between **0.4%** and **0.9%** of the previous year's net revenue budget (NRB). The MTFP as approved in February 2020 included an annual amount of **£1.475m** (i.e. **0.6%)**. The proposed in year savings of **£12.505m** for 2020/21 include a saving of **£1.393m** from contingency which is the remaining 2020/21 balance, therefore leaving no central contingency for the remaining 2020/21 budget period. In light of the financial operating context the central contingency value will be reviewed during the next financial year and may be reduced, in order to increase the general fund balance.

Earmarked Reserves

Earmarked Reserves are funds set aside to provide for specific future expenditure plans. The Council held balances of **£153.683m** in earmarked reserves at 31 March 2020 which includes schools budget balances of **£14.152m**. A review of these earmarked balances has been performed to establish the purpose of the reserves and the likely timescale that these reserves will be utilised.

The main categories of earmarked reserves that the Council holds:

- Sums set aside for major schemes, including Private Finance Initiatives, capital developments, or to fund transition and transformation
- Potential Liabilities
- School Balances
- Insurance and risk management
- Traded surpluses

The proposed use of reserves in year represents a **49.3%** reduction in the total of earmarked reserves. It is proposed that **£38.718m** of earmarked reserves are permanently released to deal with the financial impact of Robin Hood Energy. It is also proposed that **£31.304m** of reserves are released to deal with the in-year budget situation and repaid back over the period at which liabilities become due. Such a drawdown of reserves is significant and will have a range of significant impacts including, but not limited to:

- Significantly reduced balance sheet position
- Significantly reduced financial flexibility
- Future years impact on the MTFO due to the repayment of reserves
- Reduced ability to deal with unexpected or emergency situations in the future

Housing Revenue Account (HRA)
The MTFS requires the City Council to establish opening HRA reserves of between **2%** and **3%** of the gross HRA spend (capital and revenue) the precise level within this range being informed by the risk assessment with no opening working balance ever being set below the 2% threshold in an individual year. The working balance opening balance for 2020/21 is **£7.727m** however this is expected to be reduced by **£0.355m** by the end of 2020/21.

## Conclusions

The environment in which the Council operates continues to see unprecedented financial challenges both in terms of funding together with increased demand, uncertainty in the funding beyond 2020/21 and the significant financial impact of Covid-19. There is a number of local authorities are experiencing severe financial difficulties due to the impact of Covid-19. Setting balanced budget prior to Covid-19 was already increasing each year, however through extensive consultation with Senior Colleagues, Finance Colleagues and Executive Councillors the Council presented a balanced budget for 2020/21. It became clear as the impact of Covid-19 developed that in-year action would be required to ensure that this remained the case. The budget for 2020/21 already contained significant risks and as a consequence of the pandemic some of those risks are now issues. However, with contingencies and reserves at the level set out here and in the overall budget report, the CFO considers that the proposed Interim Budget for 2020/21 is robust and that the level of reserves is adequate. That said the medium term remains extremely difficult.

It should be noted that there remains significant budget gaps for years 2021/22 and 2022/23 and therefore a series of recommendations and actions are required as part of the current budget process in order to address these:

- Updating the State of the Nation paper in October 2020 to assist the development of a budget strategy with a stronger focus on transformation and financial sustainability as we move towards the full implementation of the requirements of the CIPFA financial Management Code. This should include creating headroom within subsequent budgets to cover potential overspending, non-delivery of savings and replenishment of reserves.
- Keep under constant review reserves, balances and provisions to replenish the resilience reserve.
- Update the MTFS with respect to the General fund opening balance range which is currently defined as being within the range **2%** to **4%**. The review is to take into account the Council's reduced budget flexibility as a result of the continued use of one off measures to reduce overspends and present a balanced budget which addresses the medium term impact of the use of reserves proposed in the Interim Budget and takes into account the on-going impacts of Covid-19, with a view to reducing the risk in the Council's budget.
- Review and update the current MTFP practices and amend as necessary to align with CIPFA Financial Management Code
- Produce an early detailed 3-year MTFP to address the budget gaps in years 2 and 3 which will require a thorough transformation plan and strategy in order to balance the medium-term financial position

This statement has been prepared in good faith and having made best endeavours to consider all known prevailing relevant issues.

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