Annex 5

Robustness of the 2021/22 Budget

Contents

Robustness of the Budget and Adequacy of Reserves

1 Introduction

1.1 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.

1.2 Conclusions of this review are shown in section 10 to this Annex

2 Overall Robustness of the Budget

2.1 The Medium Term Financial Plan (MTFP) forms the overarching framework within which the Council's financial planning and management activity takes place. The annual budget is an integral part of the rolling multi-year MTFP. This approach enables it to support delivery of the Council's priorities and services as detailed within the Council Plan.

2.2 In 2020 the financial planning context shifted considerably and the impact of Covid-19 pandemic led to the then S151 Officer implementing an Interim Budget which was approved by Full Council in October 2020 to ensure the Council had a balanced legal budget for the financial year 2020/21.

2.3 On 11th August 2020, the Council's external auditors, Grant Thornton, issued a Public Interest Report following the Council's decision not to continue to provide support to the company in the light of a deteriorating financial position. The Public Interest Report made a number of recommendations which the Council has accepted and is now implementing. https://www.nottinghamcity.gov.uk/public-interest-report/

2.4 Following issuance of the Auditor's Public Interest Report (PIR), the Secretary of State for Housing, Communities and Local Government (MHCLG) appointed Max Caller CBE in late October 2020 to lead a rapid, non-statutory review (NSR) at the Council. The purpose of the review was to provide assurance on the financial position of the Council, its governance arrangements and the commercial and investment issues identified by the Council's External Auditors, Grant Thornton, in the PIR published on 11 August 2020. The findings from the review were published in November 2020 and details can be found at https://www.gov.uk/government/publications/nottingham-city-council-rapid-review.

2.5 Key findings of the report include the need for a longer term financial planning horizon to ensure that the Council achieves financial sustainability over a 2-3 year recovery phase. Additionally, the report findings covered the Council's debt position, the lack of pace in releasing underutilised assets and governance matters for the Council and its companies.

2.6 After consideration of the report, the Secretary of State determined that the Council must produce a Recovery and Improvement Plan and that an independent Improvement Board would be put in place for a three year term to support the Council in its recovery journey, oversee the implementation of the Recovery and Improvement Plan and to provide assurance to the Secretary of State for Housing, Communities and Local Government (MHCLG) that the Council is making satisfactory progress at pace The Improvement Board is Chaired by Sir Tony Redmond with three other independent sector expects and the Leader of the Council.

2.7 The Council duly developed a Recovery and Improvement Plan which was approved at Council on 25 January 2021 and can be found at https://committee.nottinghamcity.gov.uk/ieListDocuments.aspx?CId=156&MId=8931

2.8 Central to the plan is a realignment of the Council's vision through a new Council Plan, which will align the Council's ambition to deliver modern citizen-centric services within a financial envelope which is affordable and sustainable over the medium term. This is a reforming agenda delivered with support from the Improvement Board again a clear plan.

2.9 The plan includes eight themes but four of these a directly relevant to this assessment:

- Theme one – MTFS (Medium term MTFS, a reforming transformation programme, strong spending controls and monitoring);
- Theme two – Asset Management (Asset Disposal Strategy, Operational and Community Asset Review);
- Theme three – Companies (Council Owned Company Review, Company Governance and Commercial Strategy);
- Theme four - Capital Programme (Capital Strategy, Debt Management Strategy, Review of Capital Schemes and Strengthened Programme Controls)

Each theme consists of a number of objectives, deliverables, activities, risks and actions/milestones with timescales for the actions.

2.10 The severe impacts of the Covid-19 pandemic on the City in 2020/21 will continue to have a fundamental financial impact for the medium term. An event of this magnitude undoubtedly means the Council will need to consider closely how its services should operate sustainably in the future. There remain the longstanding challenges to Council spending and revenues if citizen needs and working and spending patterns in the city continue to change. In this context it is essential that the Council deploys its resources efficiently so that it can continue providing its services to citizens, visitors, and partners.

2.11 The ongoing uncertainty of Covid-19 and the development of the Recovery and Improvement Plan has meant that it is prudent to produce only a one year budget for 2021/22 rather a medium term MTFP. This provides the opportunity to review the Council's response to the recovery phase of the pandemic, to develop a new reforming Council Plan with major service transformation and also for the findings of the PIR and NSR to be delivered and a full MTFP prepared for the period commencing April 2022.

2.12 This assessment of the robustness of the budget focuses on the likelihood that actual spending and income may vary from the 2021/22 budget, the long term financial sustainability of the Council, the impact on reserves of the current budget strategy and the subsequent impact on the financial health of the organisation. It will also include additional measures and actions implemented by the S151 Officer in response to current financial environment, recent NSR findings and Recovery and Improvement Plan.

2.13 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 due to the unprecedented impact of the Covid-19 pandemic and related lockdown. 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.

2.14 The focus for 2021/22 was to deliver a balanced 2021/22 budget in line with legal requirements rather than to deliver a medium term financial plan in the face of so much uncertainty. Following a period of intensive financial work, the Council is able to present a balanced budget for 2021/22 without significant recourse to reserves. The Recovery and Improvement programme and a refreshed Council plan will be the foundations for building medium term sustainable finances in the future.

2.15 In line with the non-Statutory Review findings, the Council is seeking Government authorisation to be able to capitalise **£35m** of revenue costs. This authorisation is not needed to balance the budget in 2021/22 but rather to:

a. Spread the costs of Covid-19, unachieved savings and Robin Hood Energy in 2020/21 over a number of years to reduce the impact on its diminishing reserves;

b. Create a Transformation Fund to enable the necessary transformation and reform to take place leading to improved service outcomes and long term financial sustainability.

2.16 The request to Government was submitted on 23rd December 2020 and at the time of writing this report, no decision has been made by the Secretary of State to grant this request. Acting prudently, the Council has therefore prepared this 2021/22 budget on the basis that consent has not yet been received for this request.

2.17 The Council will need to make some further use of reserves in 2021/22, namely

i. To balance the residual deficit on the General Fund (**£2.0m**)

ii. To fund redundancy costs inherent in the savings plan to achieve the budget proposals (**c£7.2m**)

iii. To pump prime the transformation programme to begin to make the necessary progress in delivering the Recovery and Improvement Programme

2.18 The impact of these measures, without capitalisation, would be a further depletion of its reserves and insufficient resources to meet the demands of transformation

2.19 Not having the necessary authorisation to capitalise will not impact the overall conclusions of the S151 Officer in respect of the robustness of these proposals for 2021/22 but will place considerable additional pressure on the Council's already diminished and leave it without the necessary resources to fund its critical transformation programme outlined in the NSR.

2.20 The Council will continue its discussions with Government to make the case for this necessary authorisation to be granted.

3 Financial Environment and Framework

3.1 The external framework in which the Council operates continues to be significantly challenging. The impact of Covid-19 will continue into the medium term and will lead to additional costs and reduced income. This will also be true for council owned companies whose diminished profits will result in the cessation of dividends. Together with the uncertainty over the long term impacts of Brexit, the funding envelope for local government has never been under more pressure.

3.2 Whilst the government has provided significant additional funding to address the financial impacts of Covid-19, the local impact in Nottingham of the various packages will mitigate around **63%** of the actual financial impact in 2020/21. The City of Nottingham is not unique in this respect and the impacts of Covid-19 are expected to continue into 2021/22 and beyond until there is a sustainable long term solution to fund public bodies to an appropriate level. This will continue to impact not just on the City Council, but also in the many company entities in which it has an interest.

3.3 The following section details key elements that have shaped the construction of the 2021/22 budget.

Previous Financial Performance

3.4 In recent years, Nottingham has consistently overspent against is approved budgets as a result both of increasing cost pressures and the under delivery of savings proposals:

- 2016/17 **£2.5m** overspend
- 2017/18 **£4.2m** overspend
- 2018/19 **£1.7m** overspend
- 2019/20 **£6.8m**, overspend of which **£2.9m** was directly attributable to Covid-19.

3.5 In order to mitigate the overspend as much as possible the Council has in the past extensively used one off resources and has eaten deeply into its reserves. This has only served to reduce long term financial resilience and to reduce the future budget flexibility of the Council. Covid-19 has brought out the weaknesses of this approach for both the Council and its company interests and, together with the decision to withdraw from Robin Hood Energy (RHE), necessitated an Interim Budget in 2020/21 to balance the budget – requiring significant short term unplanned savings and a considerable draw on reserves.

3.6 The 2020/21 Interim Budget as approved by Full Council in October 2020 highlighted and addressed the combined impact of Covid-19 and specific issues in relation to the decision by the Council to terminate its interests in its wholly owned energy company – Robin Hood Energy. The Interim Budget needed to address both net Covid-19 costs of **£29m** and costs associated with RHE estimated at **£38m**. Further in-year savings of **£12.5m** were identified of which **£10.3m** were one-off items or one-year savings. At the time of the Interim Budget it was also necessary to use circa **£70m** of reserves amounting to **49%** of earmarked reserves.

3.7 It is recognised that this strategy of short term financial management is not sustainable in achieving a long term financial stable Council and that the Council no longer has the resources to follow such an approach. Change is an inevitability.

Impact of using one off measures

3.8 During the last 4 years, there has been a consistent use of one off measures and mitigating management actions to manage spending rather than a long term and structured approach to financial management. The range of management actions required have included:

- reducing contingency balances
- extensive use of earmarked reserves
- reduced revenue contribution to support capital programme expenditure
- vacancy freeze controls
- cessation of non-essential spend
- reductions to maintenance spend and
- restrictions on travel and conferences

3.9 The continued use of reserves and one off measures to address budget shortfalls has had the impact of detracting from making the more significant transformational changes that are required to secure the City's medium-long term financial sustainability. Whilst government policy encourages councils to utilise reserves to help manage the financial impact of Covid-19, the excessive use of these resources on top of regular damaging short term savings presents a significant threat to Nottingham's overall financial health. It needs to be recognised there are significantly diminishing opportunities for the repeated use of one-off measures and the budget flexibility of the Council is now severely limited.

2018/19 External Audit – key issues and recommendation

3.10 The 2018/19 and 2019/20 external audits have not yet been concluded. However, the 2017/18 external Audit reports 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."

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

3.11 A significant component of previous budget strategies has been 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 and will continue in the medium term to have a disproportionate impact on the financial health of the Council and its associated companies due to the previous reliance upon income as part of the Council's MTFP.

3.12 These income assumptions have been reviewed as part of the budget process and the draft budget includes income pressures direct resulting from Covid-19 of **£16.8m** in 2021/22. This reduces to **£8.5m** in 2023/24 but demonstrates that the impact of Covid-19 on the Council's income is forecast to be significant over the medium term.

CIPFA Financial Resilience Index

3.13 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.

3.14 The latest information includes data from the financial year 2018/19 and shows that Nottingham is carrying above average risks in the following areas:

- Has a high level of Interest Payable relative to the size of its budget.
- Has a high level of gross external debt.
- Spends a higher proportion of its budget on Social Care services compared with its peers.
- Has a limited ability to raise revenue from Council Tax when compared to others because it has a far higher proportion of Band A and B properties than its comparators (and thus a lower proportion of Band F, G and H)
- Has a low level of reserves relative to its budget in relation to comparators
- Has used its unallocated reserves more quickly than comparator groups.
- Has a higher proportionate spend on Children's Social Care services than others in the comparator groups
- Has a higher proportionate spend on Adults Social Care services than others in the comparator groups

3.15 The following areas are where the Council has been assessed at a lower degree of Financial Stress risk compared with its peers:

- Holds a number of earmarked reserves however this will be reduced in future years as a result of the approved Interim Budget
- Has a relatively high level of fees and charges to fund its revenue requirements.
- Carries significant earmarked reserves in relation to others (including PFI) – this will change in future results given the approved use of reserves in the Interim Budget.

3.16 The use of reserves to support the 2020/21 Interim budget has significantly reduced the Council's earmarked reserves and will therefore adversely impact on the CIPFA Financial Resilience Index in future benchmarking releases.

Symptoms of financial stress

3.17 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:

- 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

3.18 It is clear that Nottingham is experiencing all of the above to a greater of lesser degree and needs to address this through long term planning.

Public Accounts Committee

3.19 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.

3.20 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.

Fair Funding Review and Business Rates Reform

3.21 The introduction of the Fair Funding Review and a standard 75% Rates Retention has now been further delayed due Covid-19, therefore funding for 2022/23+ is unknown and the MTFO assumes funding for 2021/22 will continue for 2022/23+. Each of these has the potential to benefit the city’s finances.

3.22 The final local government financial settlement has confirmed funding for 2021/22 only and 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.

4 Internal Measures to monitor the financial performance

4.1 The need for accurate, timely and robust financial monitoring is a key priority for the Council and a number of changes have been and will continue to be implemented as the Council progresses on its Recovery and Improvement Plan. These include:

- An enhanced regime of Director and Portfolio Holder accountability through monthly budget review meetings to ensure delivery of individual savings.
- Implementation Plans for all new 2021/22 savings – agreed and signed by Corporate Directors and Portfolio Holders.
- Enhanced monthly monitoring to Executive and the Corporate Leadership Team with a focus on the timeliness of reporting.
- Regular risk based assessment of the Council’s financial position.
- Development of a Transformation Programme structure to deliver new ways of working

- Budget Manager budget packs supported by Finance Business Partners

Budget Review Meetings

4.2 Monthly Budget Review Meetings will be established in 2021/22. These monthly meetings will be led by the Portfolio Holder for Finance and the S151 Officer and will require Corporate Directors and Portfolio Holders to present the financial performance of their services, identify key risk areas and report on the progress of delivery of savings against the Implementation Plans. Where savings plans are off target, mitigations will be sought. This is particularly important in highlighting areas of budget pressures as early as possible in the process, to enable appropriate management action to take place where necessary.

Implementation Plans for all new 2021/22 savings

4.3 Implementation Plans have been introduced as part of the 2021/22 MTFP process. No savings proposals has been included within the 2021/22 budget without a duly signed plan. These plans are to give the Council and the S151 Officer the necessary assurance that the savings included within the budget are robust, credible and deliverable. These plans will form part of the Corporate Directors accountability in achieving the commitments made as part of the budget process.

Enhanced monthly monitoring to CLT and Leadership

4.4 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

4.5 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. Budget Managers are supported throughout the year by Finance Business Partners and a suite of reporting.

A new Financial System – Oracle Fusion

4.6 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 and part of this change includes the requirement for new accounting codes. Budget Managers have been supported through this transition with engagement sessions, training and budget packs. As part of this transition process Budget Managers will receive their annual budget pack presented in the new accounting codes and structure and also include a mapping from old to new codes. Oracle Payroll and HR will go live later in 2021/22 consequently there will be a short period when Finance and HR are on different systems, interim arrangements will be in place to support Budget Managers during this time.

4.7 The new Financial System in Oracle will give greater financial visibility to Budget Managers and support senior managers within the Council deliver on their budget accountability. The new system has greater integration between the Finance and HR systems however in the short term the gap in go lives will require interim reporting arrangements for the first quarter in 2021/22, Budget Managers will remain full accountable for their budgets in the interim phase.

5 Constructing the 2021/22 budget, transformational programme and financial position

Constructing the 2021/22 budget

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

5.2 Given the factors outlined in the report including uncertainties about the future operating and financial environment, it has not been position to develop a Medium Term Financial Strategy. Rather this year represents a one year budget for 2021/22 with a financial outlook for future years but without proposing specific solutions for funding gaps beyond 2021/22. The Recovery and Improvement Plan will build towards long term financial planning through programmes of transformation and reform and through a radically different approach to capital planning and management.

Assumptions

5.3 Underlying assumptions have been reviewed by the Council's S151 Officer and found to be satisfactory as follows:

- The budget has been prepared without an assumption that the Council's capitalisation request will be granted
- The provision for inflation and other grants and income 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.
- 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.
- 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
- 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

Integrated Transformational Programme

5.4 A robust transformation programme is key in achieving the long term financial sustainability. Fundamental service reform and changing to modern efficient business models of delivery for the Council to avoid further damaging one off service cuts. The Recovery and Improvement Plan will form the vehicle for delivering change. Theme one of the plan is the MTFS work stream, this will create an Integrated Transformational Programme and develop a long term funding envelope for core services and reduce the reliance on commercialism, therefore setting the affordability envelope.

5.5 The Integrated Transformation Programme will oversee and drive the key areas of service reform required across the organisation, and align outcomes to budgets to ensure that Council's objectives are met within the parameters of that envelope. The Programme Management Office (PMO) will ensure that the programme delivers in an efficient and effective way and all projects will be required to develop and deliver to Project Management Plans and Business Cases and be subject to the overall monitoring and governance regime set out as part of the wider Recovery Programme.

Current Financial Position - General Fund Revenue

5.6 The Quarter 3 2020/21 monitoring reports variances to the Interim Budget and prior to the additional Tranche 4 funding which was announced after the setting of the Interim Budget is **£4.9m** favourable, this is largely driven by favourable Care Purchasing budgets within the Adult Care and Transport portfolio. This has been offset by the impact of the latest lockdown and difficult trading environment with the Council's companies. The additional Tranche 4 funding of **£10.7m** has enabled a repayment to reserves, this will then reduce the level of reserves to be borrowed.

5.7 The Interim Budget assumed **£31.3m** of reserves would be borrowed and paid back, this is now assumed to be **£17.4m** and the consequently reduction in the repayment schedule has been assumed within the 2021/22 budget.

5.8 Spending controls remain in place for 2020/21 to ensure only essential spend is incurred. Full details of the latest position are in Annex 1 of this MTFP report.

5.9 The capitalisation request to MHCLG is intended to obviate the needs to borrow from reserves. The Council, if granted authorisation, would capitalise **£17.4m** and reserves would therefore benefit from this change. As this request has not yet been confirmed, the 2021/22 budget reflects the need to borrow from reserves with the first repayment starting in 2021/22 adding further pressures.

Current Financial Position - HRA Revenue

5.10 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 to **£7.7m** (from **£4.0m** in 2017/18)**.** The opening working balance for 2020/21 was **£7.9m** however this is expected to be reduced by **£0.3m** by the end of 2020/21 to **£7.6m**. 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.

6 Capital Programme Risk Management & Governance

6.1 The Council has developed a Recovery and Improvement Plan in response to the findings of the NSR. The report acknowledges that a sustainable capital programme, and the strategy and controls to shape and manage it, is a critical contributor to the overall financial recovery of the City Council.

6.2 It recommends a review of the capital programme which will look to stabilise the current programme and put it on a sustainable footing for the longer term. Development of an effective Capital Strategy and a strengthened governance and control framework will support the Council in achieving this. Implementation of the Plan will be a key priority of the Council and the Capital Strategy will be an important document to support the delivery of the plan.

6.3 Key activities include: -

- A full review of the capital programme to remove de-prioritised schemes and add in future liabilities
- Revised Debt Management Strategy align with Capital strategy with an aim paying down debt over time.
- Creating a revised Capital Strategy incorporating a prioritisation process.
- Delivering a strengthened Governance and Control Framework and ensuring that this is put into practice across the Council.

6.4 The implementation of this strategy will assist in the Council meeting its Recovery and Improvement Plan by ensuring that:

- Capital investment is strictly prioritised and meets the Council's objectives within a set funding envelope.
- Investment meets the CIPFA criteria of being prudent, sustainable, affordable and value for money.
- The Council is appropriately responding to the recommendations raised in the non-statutory review.
- The Capital Programme does not include any schemes that meet HM Treasury's definition of debt to yield.
- Capital projects are delivered within budget and in a timely manner.

6.5 The Council have significantly relied on borrowing to fund capital expenditure in recent years leaving the Council with significant debt exposure. To mitigate this risk going forwards the Council will seek to pay down debt, through a strict prioritisation of spending decisions and the acceleration of generating capital receipts subject to maintaining best value.

6.6 A revised debt policy is now being put in place in respect of new capital expenditure is thus as follows:

- 2020/21 – To minimise spend and borrowing subject to pre-existing capital commitments and expenditure already incurred within 2020/21. The capital Programme has been reviewed and a number of schemes been removed or rephrased. This review concluded in February 2021 and **c14.7m** of General Fund schemes were de-committed and a further **£19.4m** of Public Sector Housing schemes were removed.

- 2021/22 - To restrict new borrowing to the level of the annual debt being repaid. (i.e. New borrowing no greater than the MRP repaid). The Capital Programme has been reduced to existing commitments.
- 2022/23- 2024/25 - Nil new borrowing throughout the period. This applies both to general fund and public sector housing debt – the latter managed on a cumulative basis over the period.

6.7 The Council has adopted a new corporate process for developing a rolling multi-year capital programme. This will operate on an annual cycle with clear timescales, clear information requirements and clear evaluation criteria. The purpose of the new approach is to ensure that capital resources are directed towards supporting schemes that best meet corporate objectives and that capital projects are deliverable.

6.8 A new Capital Programme Board structure is currently being established and expected to be operational by February 2021. This Board will provide strategic oversight of the implementation of the strengthened Governance and Control Framework. This will ensure that projects only commence once they have gone through the prioritisation process, and are then subject to a support, monitoring and assurance package to improve delivery. Controls will also extend to the management of benefits post-delivery to help inform ongoing performance and future investment decisions. The Board will also oversee the delivery of the actions and recommendation set out in the Recovery and Improvement Plan

6.9 The draft 2021/22 capital budget is based on this new Capital Strategy and debt policy

Capital Programme – Current Position

6.10 General Fund – Current forecast spend, including schemes in development, is **£380.4m** and is fully funded.

6.11 **£219.4m** of grants and contributions and **£98.9m** of borrowing will be required to fund the programme as well as **£53.2m** of capital receipts, of which **£7.2m** are unsecured and revenue resources of **£8.9m**. This represents a funding risk and this practice will be discontinued from April 2021. 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.

6.12 Public Sector Housing - The forecast spend to 2025/26 is **£285.4m**.

Capital Programme Risk

6.13 The proposed five-year programme will require the Council to use a high proportion of available resources but without recourse to any more borrowing than is necessary to meet existing commitments. Investment of this nature will result in the Council being exposed to additional risks as follows:

- 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

6.14 The management of risk will be overseen by the Capital Board.

7 Companies

7.1 The Council has a range of companies in its ownership and some owned jointly with others that have developed over time. Many of these companies have experienced trading difficulties mainly arising from the ongoing economic impact of Covid-19 on business models. The MTFP includes a pressure of **£4.4m** in 2021/22 rising to **£5.9m** in 2022/23 in relation to group companies.

7.2 The Recovery and Improvement Plan includes a theme dedicated to the Council's companies. This theme seeks to reach a clear determination on the future and direction of each Council company within a coherent and effectively managed commercial strategy. It will do this by addressing the following key objectives:

- Provide greater visibility of company performance and risk profile of the wider City Council group.
- To reduce overall complexity and simplify the management and oversight of all core Council activities by reducing the number or alternative delivery vehicles.
- To strip out duplication of overhead and management costs by bringing core functions in house where there is no imperative to maintain externalised delivery vehicles.
- To identify opportunities to generate capital receipts to the Capital Programme through divestment of interests in profitable activities that are outside the City Council's core competence
- To establish robust shareholder controls and assurance mechanisms for those companies Nottingham City Council maintains.

7.3 The Recovery and Improvement Plan sets out a work programme with milestones as to how this will be achieved in 2020/21 and 2021/22.

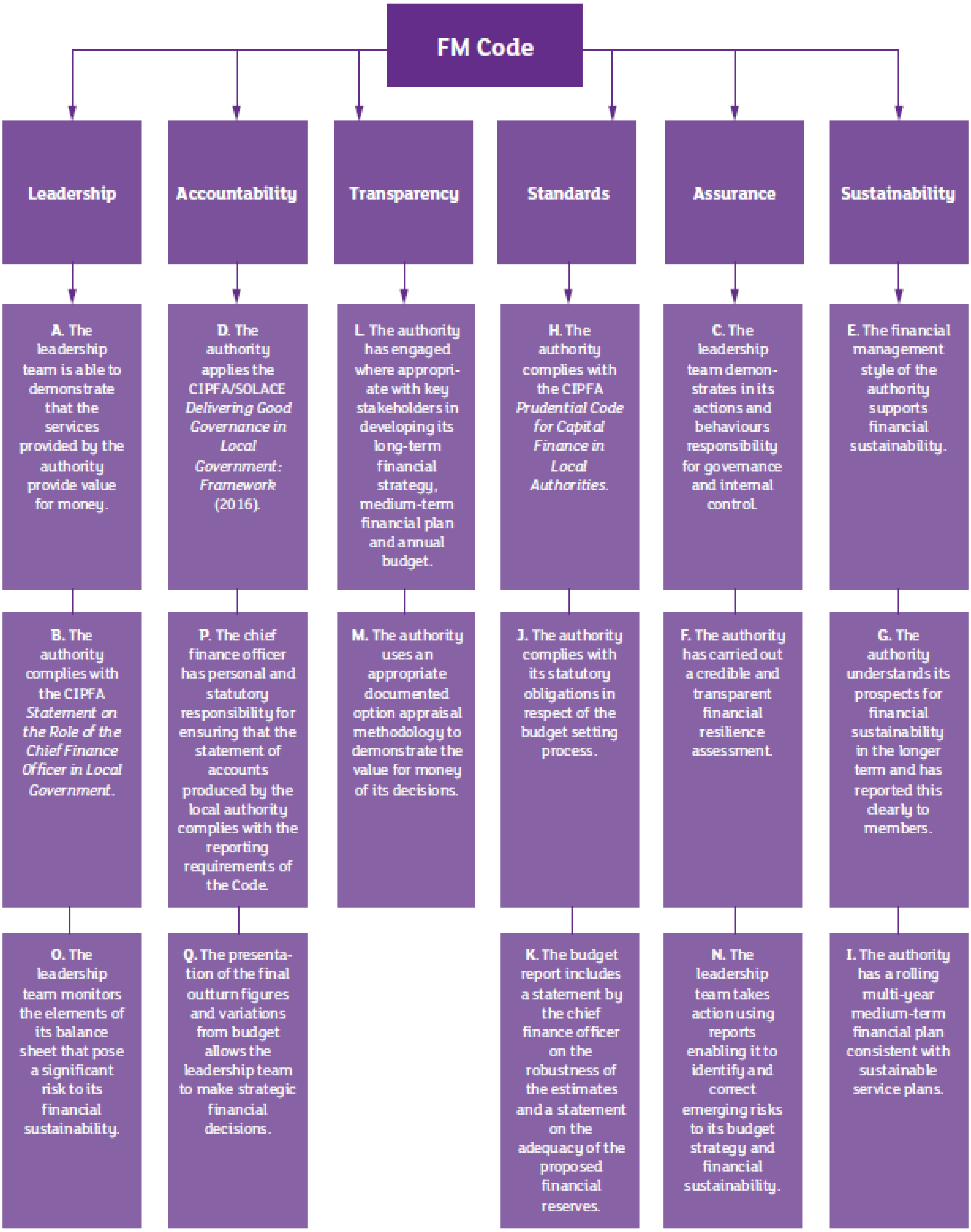
7.4 The Chartered Institute of Public Finance and Accountancy (CIPFA) has been engaged by the Council to undertake data-based review and diagnostic work on council-owned companies and those in which we have a substantial interest. The recommendations identified by CIPFA will feed into the recovery and improvement plan activities and inform the City Councils future decisions on company holdings.

8 CIPFA Financial Management Code

8.1 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.

8.2 Nottingham City Council will fully adopt the code which 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 & Financial Management



8.3 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.

8.4 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 mandatory compliance will therefore be 2021/22.

8.5 The Council will continue to assess its compliance with the new Code, many of the principles within the code have been referred to in the Interim Budget and Recovery and Improvement Plan. The paragraphs below identify the sub sections within each principle and an assessment of the Council's progress towards these requirements.

8.6 The section 151 Officer will be undertaking rigorous training for elected members, senior managers and heads of service on the implications and actions needed to meet the requirements of the code as part of a programme to enhance financial management skills and accountabilities across the organisation.

9 Adequacy of Reserves and Risk Assessment

9.1 The assessment of reserves is important in the context of the sustained cuts in funding and depletion of reserves. 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 or a failure to achieve budgeted savings is never advised, except in emergencies and/or to enable transition to new ways of working. Whilst the use of reserves to date has been deemed to be affordable, they are now at a level whereby any significant further use would leave the Council exposed to risk and unable to manage potential risks.

9.2 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: continued financial impact of the Covid-19 pandemic, increased demand for services from citizens, changes in legislation, 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.

9.3 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 Recovery and Improvement Plan and the themes and actions arising from the programme ensure that the Council can achieve long term financial sustainability.

9.4 **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 2019/20 RO returns, demonstrating Nottingham's reserve position is lower relative to similar councils.

The Council's reported figure in the RO is prior to the actions taken in 2020/21 to restore the General Fund balance to **£11.6m or 4.8% of net revenue expenditure**.

Table 1 : Comparison 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	854.2	133.0	15.6%
Leeds	546.4	31.5	5.8%
Bristol	365.5	17.0	4.7%
Sheffield	394.9	13.2	3.3%
Manchester	482.3	21.3	4.4%
Newcastle	236.4	10.1	4.3%
Liverpool	507.4	5.7	1.1%
Nottingham (See Paragraph 9.9)	**240.8**	**2.2***	**0.9%**

***£2.2m as reported within the RO returns and represents the opening general fund balance of £11.6m less the 2019/20 overspend of £6.8m and £1.7m element of the 2018/19 overspend and before the additional £1.0m increase to the general fund balance**

9.5 This assessment 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 Implementation Plans introduced for the 2021/22 budget and subsequent Budget Review meetings will support this activity.

9.6 At the time of writing this report there are national restrictions in place, and there continues to be exceptional demands upon the Council for services and it continues to be challenging for the Council to deliver services to the same level and standard. The Council's Leadership continues to lobby Government for additional financial support from central government to bridge the unfunded Covid-19 funding gap.

General Fund Balance

9.7 Previous financial plans have established a target opening balance (unearmarked reserves) on the general fund to be between **2%** and **4%** of the total net general fund revenue budget.

9.8 The level of general fund balance is expected to be sufficient to support financial risks in a single year budget. However, recent events have demonstrated that circumstances can arise which, if they occurred, could exceed the un-earmarked reserves and require further action. The most pressing issue in relation to this is the longer term financial 'scarring' from the Covid-19 pandemic over and above what has been factored into the 2021/22 budget.

9.9 The general fund balance has been informed by the detailed risk assessment undertaken as part of the budget process. The Interim Budget addressed the 2019/20 overspend of **£6.8m** to restore the general fund balance to the level assumed in the February 2020 approved MTFP of **£11.6m (4.8%)** and this represented a **£1.0m** increase from 2019/20 in light of the additional risks. The 2021/22 budget assumes an increase of **£1.0m** pa for the duration of the budget, which would increase the opening general fund balance to **£12.6m** (**5%)** of the general fund budget.

General Contingency Budget

9.10 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 proposed level for 2021/22 is **£1.5m** (i.e. **0.6%)** and takes account of the significant savings package and challenging future financial outlook. 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

9.11 Earmarked Reserves are funds set aside to provide for specific future expenditure plans. The Council held balances of **£153.7m** in earmarked reserves at 31 March 2020 which includes schools budget balances of **£14.2m**. 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.

9.12 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

9.13 The Interim Budget approved the permanent release of reserves of **£38.7m** and together with other movements represented a **49%** reduction in the total of earmarked reserves. The Interim Budget further approved the borrowing of **£31.3m** of reserves to deal with the in-year budget situation. The announcement of the Tranche 4 Government funding for Covid-19 together with the Qtr3 forecast reduces this borrowing requirement to **£17.4m**. These are to be repaid back over the period at which liabilities become due.

9.14 The amount of reserves to be borrowed and paid back has reduced however remains 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

9.15 Should the Council's request for capitalisation be granted, this would eliminate the need to borrow from reserves and allow the Council to spread these costs over a longer period of time.

S151 Officer approval for all movements within controllable Earmarked reserves

9.16 Earmarked reserves include reserves held on behalf of other organisations, for example Schools, and therefore outside of the definition of controllable reserves. In response to the depletion of controllable earmarked reserves as part of the Interim Budget since September 2020 all movements in reserves require S151 / deputy S151 Officer approval and no decisions around the usage of reserves can be taken without this prior approval.

9.17 The need for long term financial sustainability and the need to replenish reserves has led to the need for further changes in how controllable earmarked reserves will be managed from 1 April 2021. From this date, with the exception of specific risk reserves the remaining balances on the controllable reserves will be amalgamated and any movements from this balance will be subject to a prioritisation process and all previous decisions on the use of reserves will need to be reviewed and any short term pressures arising from this change in policy will need to be reviewed as part of the 2021/22 budget monitoring. Each drawdown request from the amalgamated balance will need a justification as to why the resources cannot be found from existing departmental budgets.

Housing Revenue Account (HRA)

9.18 The MTFS requires the 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 **£7.7m (7%)** however this is expected to be **£7.9m (7%)** by the end of 2020/21.

10 Conclusions

10.1 The environment in which the Council operates continues be one of unprecedented financial challenges arising from the pandemic, demand pressures and weak commercial trading conditions The outlook beyond 2021/22 remains uncertain and during this period, the Council will need to undergo significant reform to ensure that its ambitions are matched by its available resources.

10.2 A number of events have occurred in 2020/21 all of which have informed the assessment of the robustness of the budget and adequacy of reserves. The findings in the reports consistently point to areas of improvement which are within the Council’s control have been documented throughout this report and its supporting annexes. These include:

- Public Interest Report (PIR) published in August 2020
- Interim Budget approved by Full Council in October 2020
- Rapid Non Statutory Review (NSR), results published in November 2020
- Capitalisation request to Government in December 2020
- Recovery and Improvement Plan approved by Full Council in January 2021 and establishment of the Improvement Board

10.3 Setting a balanced budget prior to Covid-19 was already challenging in the context of long term government funding reductions and the Council’s proclivity to short term savings, a reliance on commercialisation and the overuse of reserves. Covid-19 has merely enhanced cost/income pressures and exposed weakness in the Council’s strategy in the face of a severe event such as a global pandemic.

10.4 The focus for 2021/22 was to deliver a balanced budget in line with legal requirements rather than to deliver a medium term plan in the face of so much uncertainty. Following a period of intensive financial work, the Council is able to present a balanced budget for 2021/22 with significantly less recourse to reserves than in previous years. The Recovery and Improvement programme and a refreshed Council plan will be the foundations for building medium term sustainable finances in the future. The Improvement Board will provide support and guidance to the Council as well as assurance to the Secretary of State.

10.5 In line with the non-Statutory Review findings, the Council is seeking Government authorisation to be able to capitalise **£35m** of revenue costs. This authorisation is not needed to balance the budget in 2021/22 but rather to:

a. Spread the costs of Covid-19, unachieved savings and Robin Hood Energy in 2020/21 over a number of years to reduce the impact on its reserves;

b. Create a Transformation Fund to enable the necessary transformation and reform to take place leading to improved service outcomes and long term financial sustainability.

10.6 The request to Government was submitted on 23rd December 2020 and at the time of writing this report, no decision has been made by the Secretary of State to grant this request. Acting prudently, the Council has therefore prepared this 2021/22 budget on the basis that consent has not yet been received for this request.

10.7 As set out in paragraphs 2.16 and 2.17, the Council will need to make use of c£11.2m of reserves in 2021/22. The impact of these measures, without capitalisation, would be a further depletion of its reserves and insufficient resources to meet the demands of transformation

10.8 Not having the necessary authorisation to capitalise will not impact the overall conclusions of the S151 Officer in respect of the robustness of these proposals for 2021/22 but will place considerable additional pressure on the Council's already diminished and leave it without the necessary resources to fund its critical transformation programme outlined in the NSR.

10.9 The Council will continue its discussions with Government to make the case for this necessary authorisation to be granted.

10109 The contingencies and reserves at the level set out here and in the overall budget report, the CFO considers that the Budget for 2021/22 is robust and that the level of reserves is sufficient but close to being inadequate. That said the medium term remains extremely difficult and gaining cashable savings from the Transformation Programme and wider Recovery and Improvement Plan will be critical for the long term financial sustainability for the Council.

10.11 Whilst the revenue budget for 2021/22 is balanced, the position from 2022/23 onwards is not and in order to present a balanced position further savings from the Transformation Programme and workforce savings of **£22.5m** in 2022/23 rising to **£25.0m** in 2023/24 are required. Without capitalisation, the Council would be poorly placed to undertake the necessary transformation to be able to tackle the identified gaps in future years or meet the expected costs of redundancies beyond 2021/22.

10.12 In concluding that the budget being proposed is robust and that the level of reserves is adequate for 2021/22, this statement is predicated on a series of recommendations and actions, these being:

- Align the future MTFP to the new Council Plan work streams and to the themes identified within the Recovery and Improvement Plan. This is required to achieve long term financial sustainability.
- Update the budget proposals should a positive the decision be obtained from Government regarding the **£35m** Capitalisation request.
- Amalgamation of all remaining non risk controllable earmarked reserves from the start of 1 April 2021, any movements of this reserve to be subject to S151/ Deputy S151 Officer approval and subject to a prioritisation process and to replenish the resilience reserve.
- Replenishment of the resilience reserve in order to balance any future risks associated with having a budget assessed by the CIPFA Resilience Index of having a little budget flexibility.
- Increase the general fund balance to **£12.6m** from April 2021 and to increase by **£1.0m** pa for the period of the MTFP.
- Review and update the current MTFP practices as necessary to align with CIPFA Financial Management Code

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

Clive Heaphy
Strategic Director of Finance and Section 151 Officer
Nottingham City Council

February 2021