Report of the Chief Finance Officer on the robustness of the budget estimates, adequacy of the Council's reserves and risk 2023/24

Introduction

Section 25 of the Local Government Act 2003 places a duty on the Chief Financial Officer to make a report to the Council on the robustness of the budget estimates and the adequacy of the Council's reserves. The Council must have regard to this report when making its decisions about budgets and council tax for the forthcoming year.

Robustness of Budget Estimates

Each year, the Finance team hold conversations with budget managers and look at every line item in each service area. This is important not only to check and challenge expected expenditure and income generally but helps to make sure that all assumptions are specific and targeted and take into account the individual terms on every contract. This has been particularly important this year where contracts may have RPI or CPI clauses which have increased costs well above what we'd normally expect to see year on year.

Anyone looking at our budget monitoring report for Q3 this year might be entitled to say that last year's budget has proved rather inaccurate in the face of current year's results. The reality of budgeting is that we can only ever base it on what we know and can reasonably estimate. In 2020 we set a budget in February and by March found ourselves in the grip of a global pandemic. At the point that particular budget was set, we couldn't have conceived of not being able to go to work, meet others socially, pursue our hobbies or walk into a shop. Council workers joined others on the front line to provide additional emergency support. We unexpectedly found ourselves administering tens of millions of pounds in grant funding at high speed and life as we knew it was altered in virtually every respect for everyone. In the middle of that year we reforecast our financial position and changed our short term view on our budget. In the following year, as the external situation improved gradually we set our next budget and I'm proud to say that proved pretty accurate. It took into account everything we knew was happening and we were proactive and demonstrated good financial control. This year's results are very much out of line with where we expected to be when we set the budget at the start of the year, or even started drafting it in the autumn of 2021. They are however in line with our budgeted expectations for next year and therefore endorse to some extent the accuracy of our projected numbers in the context of the situation we find ourselves in.

When I wrote this same report last year, it advocated caution because we knew that revenues were still down, that some areas such as leisure had still not recovered and that we were expecting, what we thought then were significant rises, in utility costs. It was however a cautiously optimistic report that talked about the expected post pandemic recovery and the work that each team was doing to aid that. The expectation was that, as our residents and businesses returned to a more pre pandemic life, our budget would recover accordingly with tenant businesses for example who we had worked closely with during Covid to manage rental payments, returning to their previous strong levels of commercial activity. What we did not expect and could not have anticipated was a war that would have far reaching effects on fuel and utility prices and a series of economic shocks resulting in unprecedented levels of inflation.

In last year's report I talked about how the Ubico Waste Service contract had increased by £300k year on year. This year, due to the huge increases in fuel costs and an increase in wages, especially for lower salaried staff, the year on year increase is £750k. Publica, who deliver the bulk of our services for us have also had a wage increase. This was again weighted towards lower paid staff so while it averaged out at around 6% which was significantly less than inflation, this still increased our budget by £500k. Our other key source of income, our Leisure centres, have not recovered from the pandemic. The same huge growth in utility costs that our residents and businesses are struggling with have hit our centres hard and, coupled with a hugely reduced footfall, the ability for those centres to carry on providing the expected levels of funding to support the Council's services going forward is significantly jeopardised.

The Council has several streams of income.

- There are Business Rates and Council Tax – the latter of which we are only permitted to increase by either 3% or £5 on a band D property. We have opted for the latter since it's marginally more but, due to the fact that we've always sought to maintain a very low level of Council Tax for our residents, this increase is relatively small in terms of our overall budget – although we always recognise that any increase has an impact on our residents. In the case of both Council Tax and Business Rates, the District Council retains only a relatively small portion. Most of what residents pay is passed on to Central Govt, County Council and other organisations like the Police. We are the collection authority who administer the process on their behalf.
- There are chargeable services – but many of these have rates that are fixed by statute and we recognise that where we do have flexibility, we have to consider each item carefully to avoid putting more pressure on residents who are also currently struggling with the cost of living. We do offer some non statutory services on a more competitive commercial basis such as trade waste, which gives us the opportunity to generate additional funding for other services.
- We have grant funding from central Government and each December we wait to see how much we will be given for the coming year – but don't know what the figure will be until then and receive no guarantees of any amounts beyond that. While this is not our only source of income it forms a significant enough portion that this lack of assurance brings a huge amount of uncertainty and hampers our ability to plan beyond the very short term. Last year we were forecasting a £1.6m surplus but knew that we needed to try to reduce our baseline budget so that future drops in funding could be accommodated. This year our funding has remained at the same level but our baseline budget is no longer supported by it and is in a deficit position that further inflation, even at lower levels, is expected to widen.
- The final source of income is through investment. This is one of the only areas where we can exercise some control over the amount of revenue generated but there are significant restrictions placed on us by Govt around what we are allowed to invest in and the doubling of interest rates for borrowing this year has made it much more difficult to find investments that give an appropriate level of return over and above the cost of capital.

I described our budget for 2022/23 as a "hopeful post pandemic" one and cautioned that while we had less uncertainty than previously, the local economy was still in recovery, the requirements placed on us for support had not stopped and we were still dealing with a situation that to a large extent was beyond our control. Instead of the hoped for recovery we have seen huge inflationary pressures and our residents suffering a Cost of Living crisis.

We have tried to be neither optimistic nor pessimistic in our budget for next year. Each line item has been discussed with the relevant budget holders from each service to reach as realistic a forecast as we can make. The approach, as always, has been detailed, prudent and diligent, so again I will say that the budget is as robust as it is possible to make it in the current circumstances and will be monitored carefully through the coming financial year, with corrective action taken where possible and as necessary.

I can confirm that the budget estimates, as presented, are both prudent and robust.

Adequacy of the Council's Reserves

The Chartered Institute of Public Finance and Accountancy (CIPFA) have issued guidance on local authority reserves and balances. It sets out three main purposes for which reserves are held:

1. A working balance to help cushion the impact of uneven cash flows and avoid unnecessary borrowing.
2. A contingency to cushion the impact of unexpected events or emergencies.
3. A means of building up funds to meet known or predicted liabilities, known as earmarked reserves.

The Council expects to hold general fund balances of just under £13m at the 31st of March 2023. Thanks to careful and prudent management, this is a favourable position compared to many Councils but the MTFS shows that only very short term comfort can be derived from it.

The significant change in this year's position is the move from a budget surplus to a budget deficit position.

In previous years, we have always had more funding and income than we needed, generating a surplus. This surplus is important because it gives not only protection but flexibility. If we reach the end of the year in a surplus position we can choose what current priority to spend it on. We've seen good examples of this in recent years where in 2020 a £650k budget surplus was used to fund a series of 2 year Covid related initiatives and we are currently delivering a set of initiatives around Council priorities with £750k of surplus predominantly generated from the 2021/22 results.

If we have an unexpectedly bad year like the current one where unforeseen cost increases have caused overspends in every area, the forecast surplus provides an in year buffer to absorb this financial shock before it becomes a drain on reserves.

Each time we grow the baseline budget, we put ourselves in a position where, instead of surpluses, which are often driven by unreliable grant funding, being a discretionary spend to address a current need, they become something we need to rely on for core activities and therefore fluctuations in that funding threaten that core. In short, we move from being able to make active decisions on surplus cash to being forced to make reactive decisions on deficits.

The Medium Term Financial Strategy (MTFS) at Annex E of the budget paper shows the potential consumption of our reserves over the next three years. The nature of government funding, which is currently confirmed in single year allocations, means that much emphasis is placed on the expected outcome of the next financial year. The MTFS is designed to look beyond that horizon so that longer term action can be taken.

Guidance from CIPFA and, common sense would indicate good practice, is to look not only at the amount of reserves held but also the rate of depletion. While best endeavours are used to estimate future years we do not have certainty and the position projected could be better or worse than shown. The key drivers of this uncertainty, along with potential mitigations where possible, are discussed below.

- One of the key risks in our current and future financial position is the income we hope to earn from our leisure centres. Pre pandemic, the revenue earned from some activities was able to subsidise underutilised or loss making elements of the service and still generate surplus income to support other services. During the pandemic when the centres were closed, people changed their habits and found other ways to exercise and with the cost of living now so much higher than before, many people are having to cut any optional spend in order to prioritise more basic needs. It's still vitally important that the Council is able to offer facilities for the health and wellbeing of residents. Without our centres it would be almost impossible for most people to learn to swim but swimming pools can account for 80% of the utility cost in a centre so the current rise in costs has hit our centres disproportionately hard compared to smaller private gyms without pools. We currently have short term consultancy work in progress to help us redesign our service, refining it into something that fits the needs of residents going forward and is financially sustainable. The hope then is to engage less expensive resource to support our operators in implementing the required changes and monitoring to ensure we achieve the required outcome. This represents a risk of around £2m per annum in our budget when we add the potential lost revenue to the rise in utility costs.

- In other areas where we are competing with the private sector to deliver non statutory services we need to review to ensure that they are delivering a profit against the cost of providing them. This work has already begun in several areas but needs more resource to move forward. This may seem like additional cost but if optional services are not profitable they must either be made profitable or stopped as they should not be allowed to endanger core statutory services.
- Our government funding has always been unpredictable. This is a common concern and complaint from all local authorities and one frequently raised with government. The fragility of our funding position means that we will always struggle to have assurance around any long term service provision dependent on it. While we lobby government for a longer term view on funding, we must find ways to reduce costs and increase income where we can in order to decrease our reliance on it. As discussed above, having a baseline budget that relies on transient grant funding introduces significant risk and means that any unexpected costs must be paid for from reserves.
- In 2020 the Council set out an ambitious investment strategy. It was hoped that the income earned from that would be sufficient to close what, at that time, was our projected budget gap. In the few years since then we have taken every opportunity to invest appropriately in order to achieve that but with our baseline budget rising by just over £2m this year, viable investments in short supply and borrowing interest rates rising, the gap has widened beyond anything that this investment strategy could hope to address. We must still pursue it as any additional income is welcome and especially revenue streams that reduce our reliance on grant funding but even with welcome additions to the portfolio such as Marriott's Walk, we recognise that this strategy alone will no longer be sufficient to close the gap that has significantly widened this year.
- As outlined above, the fact that we are now operating in a deficit means that we have taken away our access to additional money for discretional spend. Any project that is discretionary, does not at the very least cover its costs and does not deliver a statutory service, threatens and reduces our ability to deliver core services.

Most of the changes above will take time to analyse and implement. We can draw on our reserves to fill the relatively small shortfall this year but our projections show that that is only going to get worse and could potentially become significantly worse quite quickly. If we are to make significant changes, we need to do that in a controlled manner. This doesn't mean that we can delay identifying and agreeing them, it simply recognises that in order to protect services and staff, the implementation may take months. However the plan needs to be agreed without delay. Even if Govt funding was maintained at current levels for next year, we would still be operating with a deficit much larger than the current one and a risk around leisure, commercial activities and investment projections that could make it significantly worse.

I can confirm that the level of reserves is adequate in the short term, however, they are being eroded even without any expectation of additional budget growth and the rate of erosion is partly dependent on funding not within our control. Swift action must be taken to improve commercial returns where possible and identify and implement cost savings in order to support the continued provision of services. The timescales predicted in the MTFS do not allow for inaction or complacency.

Risk

Discussion is included above, and in the strategy papers, around the significant risks related to our budget and ongoing financial position.

These are primarily:

1. The recovery from the pandemic which continues to impact the Council's income streams.
2. The inflationary increases and disproportionate rises in fuel and utility costs affecting our finances and those of our residents and businesses.
3. The impact of the UK's exit from the European Union.
4. The as yet unclarified position of government funding beyond 2023/24.
5. The difficulty of finding compliant investment opportunities that both further our Council objectives and support our revenue stream.

These risks have been discussed in the paragraphs above and in the accompanying strategy papers. In previous years, the biggest risk facing the Council financially was the predicted loss of government funding. This risk remains but has now been compounded by the rising costs of service delivery turning what was a buffering surplus into an ongoing deficit which cannot be sustained. We are constantly trying to develop other sources of income to make us less vulnerable to funding cuts and cost increases, which are beyond our control but we also need to recognise that we are unlikely to be able to find sufficient revenue from these to resolve the problem. Some headway has been made but not enough to fully address the problem and protect the Council. Further plans must be developed immediately to increase income, reduce spending and find cost savings.

Summary:

I have often stated that WODC finds itself in a position that is more fortunate than many councils. Through careful management it has built up a good level of reserves but these could be depleted completely in the medium term. The Council must invest in improving commercial returns and income, identifying short term cost cutting measures and identifying cost reductions that can be implemented over the medium term. If we simply wait and hope that more funding will appear we run the risk of having to make emergency cuts if it doesn't. It is one thing to have plans as yet unimplemented, it's quite another to have them as yet unidentified.

West Oxfordshire District Council wants to continue serving and supporting our residents but in order to do that we need financial stability. It's not the chief objective of a Council to generate money in the way that a private sector business would and part of our purpose is to deliver statutory services that are not income generating, but the reality of that is that that service delivery has to be underpinned by a balanced budget and sustainable finances and we owe it to our residents, and our staff, to quickly and actively take steps to ensure that balance is regained.

Elizabeth Griffiths ACMA 10th February 2023