APPENDIX K

Report of	Meeting	Date
Chief Finance Officer	Special Council	23 February 2021

REPORT OF THE CHIEF FINANCE OFFICER

PURPOSE OF REPORT

1. To provide advice to the Council as required under s25 of the Local Government Act 2003.

RECOMMENDATION(S)

2. The Council are recommended to note the Chief Finance Officer's comments and advice under Section 25 of the Local Government Act 2003 as set out in this report and have regard to it when considering the budget proposals for 2021/22.

EXECUTIVE SUMMARY OF REPORT

3. This report is required by statute and the Chief Finance Officer should report to members the robustness of the budget estimated including how they have been constructed and the assumptions that underpin them. In addition, the Chief Finance Officer must report to members the adequacy of the proposed financial reserves.

4. This report outlines the key assumptions and risks contained in the budget and identifies that over time working balances will be increased to mitigate some of those risks.

5. Budget assumptions have been made based on the Final Local Government Finance Settlement that was announced on 4 February 2021. The Government has announced the budget will be published on 3 March 2021. Chorley Council will revert to membership of the Lancashire Business Rates Pool. In addition, the Government maintained New Homes Bonus allocations in 2021/22 however it will remove New Homes Bonus allocations by 2023/24.

6. The Government has supported the economy through the Covid-19 pandemic through various grants and other initiatives. Grants of over £37m have been made available to Chorley Council to enable it to support council services, its communities and local businesses. This investment in public services is welcomed, however Government borrowing is estimated by the Office for Budget Responsibility (OBR) to reach £393.5bn by the end of 2020/21 compared to £58bn in 2019/20. This level of public sector debt will necessarily require the Government to bring future public finances to a

more sustainable position. It is possible therefore that future Government investment in public services will be curtailed.

7. It is my view that the outcome of the fair funding review, expected for 2022/23, will result in the Government reducing funding for district councils and possibly transferring some of this to upper tier authorities, many of which will continue to struggle to fund adult social care and children's services. The uncertainty created by the new business rates regime means we must be prudent when budgeting for future levels of retained business rates, as such I have assumed pool membership in 2021/22 will not continue in 2022/23 onwards.

8. In terms of the 2021/22 budget once again all key budgets have been reworked to align with expected outturn for 2020/21 and therefore reflect the ongoing cost of delivering the current levels of service.

9. The forecast is that the budget will be balanced in 2021/22 and that the Council's **general fund balances** will be £4.0m. The general fund balance is above that of other Lancashire District Councils and is required to manage short-term one-off risks to the revenue budget. Funds continue to be set aside as earmarked reserves in 2020/21 that will:

    - support the delivery of the council's corporate strategy
    - enable the council to support its residents and businesses during the Covid-19 pandemic.
    - help mitigate some of the risks within the current and proposed new business rates system.

10. Key risks remain, in particular the forecasting of **business rate receipts** in 2022/23 onwards. The council will benefit from being a member of the Lancashire Business Rate Pool in 2021/22. However, the new 2022/23 75% retention scheme is unlikely to resemble the current pool scheme. As such the benefit in 2021/22 will be treated as a one-off and only growth that is achieved in the business rates base will be built into the base budget. It is prudent however to assume zero percent growth over the medium-term period.

11. The council continues to develop its **Capital Strategy**, this report demonstrates that the council's capital expenditure and investment decisions are taken in line with corporate objectives and take account of stewardship, value for money, prudence, sustainability and affordability. I am satisfied the report, Appendix H to the main budget report, provides this assurance to members and outlines what the strategic intent is for the council over the medium to long-term.

12. Having reviewed the underlying assumptions and commented on the position in relation to key risks and working balances I am satisfied that the budget assumptions are reasonable, the key financial risks have been considered and the budget is deliverable.

13. Further analysis of the risks to revenue and capital budgets are analysed at the end of this report.

Confidential report Please bold as appropriate	Yes	**No**

CORPORATE PRIORITIES

14. This report relates to the following Strategic Objectives and to the Council's ability to deliver its corporate plan whilst ensuring a balanced budget is achieved. The MTFS sets out how Council resources will be used to deliver those priorities.

Involving residents in improving their local area and equality of access for all	✓	A strong local economy	✓
Clean, safe and healthy communities	✓	An ambitious council that does more to meet the needs of residents and the local area	✓

BACKGROUND

15. Under the requirements of Section 25 of the Local Government Act 2003 the Chief Finance Officer is required to advise members when setting the budget as to the robustness of the estimates and the adequacy of working balances.

THE ROBUSTNESS OF ESTIMATES

16. In terms of the budget proposals, once again in 2020/21 a thorough reassessment of the budgets has been undertaken by budget holders, service managers and directors and their accountants based upon the latest information available. In terms of the key assumptions contained particularly in the 2021/22 budget these are shown in the main budget report but are summarised for convenience below

KEY ASSUMPTIONS

17. The table below shows some of the key assumptions made in forecasting forward the Council's financial position. These are analysed further in Appendix F to the budget report.

Key Assumptions	2021/22	2022/23	2023/24
Growth in Council Tax Base	0.10%	1.00%	1.00%
Increase in Retained Business Rates through Growth	0.00%	0.00%	0.00%
Total Forecast New Homes Bonus	£1.489m	£0.550m	£0.000m
Future Service Pension Rate	16.4%	16.4%	16.4%
Pension Fund Deficit Recovery	£0.432m	£0.450m	£0.466m
Additional Business Rates - Lancashire Pool 21/22 Transitional Business Rates Income 22/23	£1.139m	£0.570m	£0.000m

Pay Award	0%	2%	2%

In terms of the key assumptions I would make the following comments to confirm their validity:-

COUNCIL TAX INCREASES

18. The administration is proposing an increase in council tax of 1.99% in 2021/22. The MTFS also assumes the same increase in 2022/23 and 2023/24 however it is acknowledged that this will be revisited every year and will depend upon the outcome of the business rates and fair funding review. As expected, the growth in housing was low in 2020/21, a prudent 1% increase in the council tax base is assumed in 2022/23 onwards. These assumptions in growth are significantly lower than has been experienced in most of the previous years.

REDUCTION IN RETAINED BUSINESS RATES

19. The council will benefit from being a member of the Lancashire Business Rates Retention Pool in 2021/22. However, the 75% business rates regimes, expected in 2022/23, is unlikely to resemble the pool and therefore the council may experience a reduction in retained business rates in the medium term, for example:
    - the final scheme may change the tier splits and provide more of the retained rates to upper tier authorities
    - when the new system is reset the Government may reduce or remove the section 31 grants, these are grants that compensate councils for Government initiatives that reduce locally generated business rates e.g. small business rates relief or retail reliefs. These grants currently equate to £1.346m a year and therefore any reduction in these grants poses a large risk to the council.
    - the quantum of business rates in the system may include the New Homes Bonus allocations that the government is phasing out over the next three years.

20. The new business rates regime will dictate the quantum of business rates to be shared nationally and locally however it is the fair funding review that will dictate how this is shared out. The fair funding review is expected to generate new funding ‘baselines’ for all councils in 2022/23. How these will be calculated, and therefore how much the council will be allocated, is still not finalised however it is believed it will be based on factors such as population growth, rurality, deprivation levels and other local area adjustments such as local labour costs. The fair funding review will allocate retained business rates based on a council’s relative need to all other councils, as a result of this it is not possible for the council to conduct any meaningful analysis of the likely outcome of this review. At this stage Chorley Council will assume the benefit of pool membership, approximately £1.139m, will be permanently lost by 2023/24 as a result of the business rates and fair funding review. The budget assumes a transitional year in 2022/23 whereby 50% reduction is experienced.

21. The budget report explains the volatile nature of this particular core income stream and why accurate forecasting of future receipts is problematic. The income levels contained within the retained business rates budget are based upon a set of assumptions that may impact on the total amount collected in future years, in

particular the outcomes within the appeals process. The council has set aside over £1.4m in reserves to manage one-off fluctuations in retained business rates.

22. A final consideration to the council's retained business rates income is the potential for there to be a national economic slow-down. This is further discussed in Appendix F – General Fund Forecast Assumptions. In brief this may result in an increase in the number of appeals against rateable values as well as reducing local economic activity and therefore reducing retained business rates. The council's share of the provision for appeals will stand at approximately £2.290m in 2021/22 which is comparable to the national average.

NEW HOMES BONUS

23. The spending review announced a gradual reduction and ultimate removal of New Homes Bonus. Government proposals are for allocations to reduce as follows:
    - 2021/22 – 3 year allocation - for Chorley Council approximately £1.490m
    - 2022/23 – 1 year allocation - for Chorley Council approximately £0.550m

24. The following announcement was made with the finance settlement in 2021/22:

    The government has committed £622 million to continue the New Homes Bonus scheme in 2021-22. The scheme financially rewards councils for the number of additional new homes they built, locally incentivising housing growth and creating homes for local residents. We will soon be inviting views on how we can reform the scheme from 2022-23 to ensure it is focussed where homes are needed most.

25. As such there may be a replacement to New Homes Bonus however nothing can or has been assumed in the budget.

LOWER TIER SERVICES GRANT

26. The Government calculates every year the council's core spending power that is a combination of the council's council tax income, business rates income and new homes bonus grant allocation. For 2021/22 the reduction in new homes bonus is not offset by the assumed additional income that the council would receive if it chose to increase council tax charges by 2%. As such the government has introduced a one-off £519k grant to compensate the council in 2021/22 called the Lower Tier Services Grant. This is an un-ringfenced grant that has been included in the council's funding streams.

BORROWING

27. The council took £4.5m of temporary (3 month) borrowing in 2020//21 to ensure the council managed its cash balances at the beginning of the pandemic. The council also secured a temporary £6m overdraft. Since then the council has managed its cash balances without the need for further borrowing.

28. So long as the internal cash position remains positive the council will temporarily continue to internally finance some of the debt required rather than borrow. The rationale for this approach is that the interest earned on deposits is significantly less

than borrowing costs and in treasury management terms is financially advantageous to the council. However, I need to be able to respond to what happens in the financial markets and as borrowing rates fluctuate be able to react. If rates are forecast to change it will be appropriate to take on some additional borrowing. For this reason, although I have built in some savings, I have also left some headroom for in year borrowing.

29. The treasury implemented a 1% increase in PWLB borrowing in 2020/21 however this increase has been reversed for 2021/22 and with it is brought a number of reforms. The largest change is that the council will no longer be able to borrow from PWLB if it has <u>any</u> investment in its capital programme for purely commercial reasons. This is not a risk to the council's current capital programme as all investments have other non-commercial objectives. However, moving forward, this will prohibit the council from investing anywhere in its capital programme purely for investment returns.

PENSION FUND CONTRIBUTIONS

30. As part of a triennial pension review the Lancashire County Pension Fund announced an increase in employer pension contributions for 2020/21 to 2022/23 to meet the future costs of the scheme. The contributions have increased from 14.4% to 16.4% resulting in an increase in the council's contribution. The same contribution rate is assumed for 2023/24 although this will be reviewed when the new three-year review is undertaken.

PAY AWARD

31. The Government spending review announced a pay freeze in 2021/22 for the majority of public sector staff with a guaranteed a pay rise of at least £250 for all staff that earn less than £24,000 per year. These assumptions have been included in the pay budget for Chorley Council in 2021/22 although these Government proposals are not yet agreed with public sector unions.

32. The spending review also announced that national living wage will rise from £8.72 to £8.91 an hour and will be extended to workers aged 23 and over from April 2021 This will not affect Chorley Council's pay bands for 2021/22 as the council pays above this level already.

33. Looking further forward, the budget includes a 2% pay increase for all staff in 2022/23 and 2023/24. This assumption adds approximately £200k to the pay budget each financial year.

MEDIUM TERM FINANCIAL STRATEGY

34. The MTFS sets out the Council's plans to bridge the funding gap as summarised below:

Chorley Borough Council Transformation Programme

	2021/22 £m	2022/23 £m	2023/24 £m
GROSS BUDGET DEFICIT	**0.881**	**2.976**	**4.168**
Efficiency Savings			
Shared Services – Phase 1 (Approved)	(0.148)	(0.148)	(0.148)
Shared Services – Phase 1 (Next Phase) Forecast	(0.040)	(0.220)	(0.220)
Shared Services – Phase 2 Forecast	(0.149)	(0.179)	(0.179)
Income Generation			
Market Walk Extension	(0.100)	(0.150)	(0.150)
Primrose Retirement	(0.74)	(0.080)	(0.078)
Strawberry Fields	0.223	(0.000)	(0.149)
TVS	(0.450)	(0.450)	(0.450)
NET DEFICIT / (SURPLUS)	**0.143**	**1.749**	**2.794**
Council Tax Increase – 1.99% 21/22, 22/23 & 23/24	(0.143)	(0.292)	(0.447)
Parking Income	0.000	(0.200)	(0.200)
Investment Sites	0.000	(0.200)	(0.400)
TOTAL SAVINGS & ADDITIONAL INCOME	**(0.143)**	**(0.692)**	**(1.047)**
REVISED DEFICIT / (SURPLUS)	**0.000**	**1.057**	**1.748**
Directorate Savings	0.000	(0.318)	(0.513)
Future Efficiency Savings & Income Generation	0.000	(0.739)	(1.235)
REVISED DEFICIT / (SURPLUS)	**0.000**	**0.000**	**0.000**

35. The strategy shows that broadly speaking the administration will attempt to bridge the gap by 2023/24 through generating efficiency savings and additional income of £4.168m. The council expects to generate £827k per annum net income from its recent investments by 2023/24. Further analysis of the risks associated with these investments, as well as other risks, are given in Appendix H – Capital Strategy Report.

36. The council will continue to build on its success with a £200k net income target from investments site in 2022/23. Despite the effects of the pandemic, I believe this to be achievable given the number of different income generating projects the council has in development. There remains preparatory expenditure to bring investment sites forward and this is why there is £326k of resources in an earmarked reserve specifically for investment in income generating projects. New posts have been recruited to and external expertise commissioned to drive forward the expansion of income generation.

37. The greatest budget challenge for the council is to generate £1.748m of efficiency savings by 2023/24. Directors have identified potential savings of £513k leaving a forecast target of over £1.235m further savings and additional income. This target is dependent upon the outcome of the funding review that is expected in 2022/23 as well as the council pursuing other measures to meet the budget gap, such as increasing council tax. £1.235m represents approximately 10% of the staffing budget. Significant savings have already been identified from the first phase of shared services and both councils are looking to expand these arrangements.

LEVELS OF RESERVES

38. The target level of general fund reserves is £4m over the medium term. This is higher than general fund balances at most Lancashire District councils and importantly the MTFS does not rely on utilising balances to meet deficits over the three-year period. General fund balances are there to manage potential risks contained in the budget particularly around:
    - the volatility in the funding system in relation to business rate retention
    - possible re-profiling of savings and income generation proposals into future years
    - risk of loss of deposits should a future banking crisis occur

39. There continue to be risks to revenue budgets surrounding the major capital projects including Strawberry Fields and Market Walk. Further analysis is provided in Appendix H – Capital Strategy - to this report. The council's budgets have been adjusted to account for the forecast temporary reductions in occupancy rates at these council owned commercial properties. I deem the general balances of £4m is prudent given these risks. In addition, the council holds earmarked reserves such as income equalisation reserves to help manage large one-off reductions in income at its investment sites.

IMPLICATIONS OF REPORT

40. This report has implications in the following areas and the relevant Directors' comments are included:

Finance	✓	Customer Services	
Human Resources		Equality and Diversity	
Legal	✓	Integrated Impact Assessment required?	
No significant implications in this area		Policy and Communications	

COMMENTS OF THE STATUTORY FINANCE OFFICER

41. These are contained within the report.

COMMENTS OF THE MONITORING OFFICER

42. The report is designed to ensure that the relevant legislation is complied with in terms of Statutory Officer advice.

JAMES THOMSON
DEPUTY DIRECTOR OF FINANCE (s151 Officer)

There are no background papers to this report.

Report Author	Ext	Date	Doc ID
James Thomson	5151	12/02/2021	

RISKS TO MEDIUM TERM FINANCIAL STRATEGY

The Medium-Term Financial Strategy outlines how the Council will achieve its corporate strategy priorities whilst recognising the budgetary pressures it will experience over the coming 3 years. Within the strategy are a number of risks that are outlined below.

RISKS TO REVENUE BUDGET

HIGH RISK

75% Business Rates Retention
The government continues its ambition to implement a new 75% business rates retention scheme for all local authorities by 2022/23. The council will continue with the Lancashire Business Rates Pool in 2021/22. Forecasting the effects of the new 2022/23 retained scheme using prior year data is challenging for the following reasons:

- The local preceptors should receive more of the locally generated business rates (from 50% to 75%) however, the government may introduce a less favourable split between lower and upper tier authorities
- The level of locally generated business rates may be reduced if the government reduces its allocations of section 31 grants – grants used to compensate councils for Government policies that reduce business rates e.g. small businesses and retail reliefs
- The current pool uses historic baseline funding levels however, the result of the government's fair funding review will see this baseline adjusted with the potential for Chorley Council to receive less of its retained NDR income.

The government continues to develop the fair funding review and new business rates system however it remains uncertain when the new system will be introduced. There remains a lot of work to be completed by the Government including the need to develop transitional arrangements. After this a consultation exercise will need to be undertaken. The budget is prudent and assumes implementation of the fair funding review and 75% business rates regime in April 2022 however this is far from certain.

Post-Covid Recovery
The pandemic has impacted on the council finances as well as the wider economic environment. This has created more uncertainty in the early stages of the MTFS. To mitigate this risk the Government has provided £1.634m (20/21) and £0.557m (21/22) of unringfenced funding. The council will also receive compensation for loss of some fees and charges for April to June 2021 and is also able to spread any council tax or business rates deficits in 2020/21 over the next three years (as opposed to the usual one year).

To help manage this uncertainty the council will create, from the Government grant funding, a Covid Recovery Fund of up to £300k to support local businesses and communities.

The MTFS has in place some funds to help the council manage the Covid recovery period however the full medium-term impact of this recovery is not yet clearly understood. This could yet impact further on council expenditure, income and Government funding levels.

MEDIUM RISKS

Business Rates Appeals and Other Business Rates Adjustments
The council's share of the provision for business rates appeals stood at £1.850m at the beginning of 2020/21 and allowance has been made for additional provision of £0.440m during the year. Of this, during the year there has been approximately £25k of successful backdated appeals charged to the provision.

In April 2017 a new business rates appeal process was introduced called 'Check, Challenge and Appeal'. The benefit of the multi-stage process is that it requires businesses to complete its own 'Check' and therefore should discourage speculative appeals. To date there has been no successfully challenged appeal reported by the VoA against the 2017 list. The VoA has focussed on clearing the backlog of prior year appeals and so it is prudent to assume more appeals will be coming through from the 2017 list in 2020/21.

Recently a number of press reports stated that the VOA had agreed a 25% rebate in office rates, worth around £481m nationwide, due to the impact of the pandemic. The argument for the rebate is that due Covid the office sector have experienced lower demand, realise lower rental values and as a result have lower rateable values. No agreement has been made with the VOA however it is understood it is in discussions that cover a number of property types. The council has 536 offices with rateable value of £8.5m. This highlights the potential volatility of the business rates system and is why the council must be prudent when setting aside reserves and provisions to manage this income stream.

The budget for 2021/22 includes further additional provision of £0.440m. This is deemed sufficient to meet the potential successful appeals that may transpire from the outstanding lists.

Pay Inflation
The Government has proposed a pay freeze for Council staff in 2021/22, except for those on lower pay, and this has been assumed in the budget. Negotiations with the employee unions is not complete and so it is possible a higher pay settlement may be approved. Every 1% increase in pay results in over £100k of additional expenditure to Chorley Council. An average 2% pay increase per year has been assumed for 2022/23 to 2023/24.

Universal Credit
The Government is consolidating a number of welfare benefits into a revised Universal Credit Scheme. One of these is housing benefit which is currently administered by the Council. Universal credit will be managed by the Department of Work and Pensions. The full scheme was rolled out in Chorley in July 2018 however take up has been slow. There is the potential risk that bad debts will increase when people move to UC as it becomes more difficult to recover overpayments. This is because the housing benefit element of debt might not have the same priority over other debt recover such as fuel or rent arrears. We have seen an increase more over the last 12 months from HB to UC as take-up has increased and therefore, there is a possibility that the council's bad debt provision will need to be increased with a subsequent charge to the general fund.

Delivery of Budgeted Savings and Additional Income
The MTFS includes forecast cumulative gross budget deficits of £2.976m and £4.168ms in 2022/23 and 2023/24 respectively. Balancing the budget will require a change in organisational culture, enhanced sharing of services across organisations and further capital investment in income generating schemes. The monitoring and robust challenge of all proposals is overseen by the council's Shared Services Management Team and Shared Senior Leadership Team. Risks are reported to Shared Services Management Team. as well as members and actions taken when required. Given the council's likely increased dependency on generating income there will always be some risks that sit outside of the council's control and are therefore more difficult to manage.

The council's general fund balance of £4m has been set such that potential delays in bringing forward income or generating savings can be temporarily managed within council resources.

As noted in the report the council is still able to borrow from PWLB at low rates to fund its capital programme. However, Government reforms have meant that in order to utilise these funds the council is prohibited from investing anywhere in its capital programme purely for investment returns. Although this will not affect the council's current capital programme, it will reduce the scope of investments the council can pursue in order to generate income and therefore balance future revenue budgets.

Existing Income
The major income streams the council benefits from include planning, garden waste subscriptions as well as commercial income from assets the council owns. Uncontrollable reductions in income could leave services under-funded. The council has been prudent when budgeting for income and has set aside an income equalisation reserve for Market Walk and Logistics House.

LOW RISK

Inflation
The council's expenditure is subject to annual inflation based on indexation that is determined by external stakeholders. Sharp increases in inflation would result in higher day to day expenditure and possible budget overspends. Inflation forecasts from the Office of Budget Responsibility (OBR) have been used to inform the budget over the coming 3 years. The OBR forecasts inflation to remain below the Bank's 2% target rate until at least 2025. Inflation is only applied to specific council contracts including the waste collection contract. This will be reviewed annually to ensure budgets are sufficient to meet inflationary pressures however it is expected that inflation will remain low throughout the MTFS period.

RISKS TO CAPITAL BUDGET

MEDIUM RISKS

Overspends on Capital Projects
All capital projects are monitored on a quartlery basis, with the major capital projects monitored on an ongoing basis by council officers and commissioned external project managers. Any potential overspends are highlighted by the relevant project group or officer and reported to the Chief Finance Officer.

Actions plans are agreed to manage potential overspends and managed by the project officer. If necessary, financing is identified within the capital programme to meet any additional required resources. Changes to the capital programme are reported quarterly to Executive Cabinet. Changes to a capital project between these periods are taken on a separate report to Executive Cabinet or Full Council.

LOW RISK

Insufficient Financing to Delivery Capital Programme
The council continues to have a significant gap between its capital funding requirement and current borrowing levels. As such borrowing is available to the council if funding sources previously allocated to projects no longer become available.

Insolvency of Major Contractor
As part of the tender process the financial standing of each contractor has been thoroughly assessed. These checks are regularly and the council's subscription to a credit check agency provides alerts were the credit status to change.