

Appendix D- Chief Finance Officer's section 25 report

As part of this report, under section 25 of the Local Government Act, the Council's Chief Finance Officer is required to comment on the robustness of estimates and the adequacy of reserves.

The major external factor affecting the Council continues to be uncertainty over future funding.

Future funding

In the draft Local Government settlement, Government have only provided a guarantee that Core Spending Power will not fall. With additional funding being targeted towards social care and areas with higher derivation, this is the situation that the Council finds itself in. The guarantee is only in cash terms (i.e. no provision for inflation) and is applied after increase in the rate of Council Tax. This is what was implied in the policy statement as well, so is a reasonable base for planning beyond 2025/26.

The policy statement provided a clear direction that there will be a 3-year settlement for the period from 26/27 to 29/30. However it is feasible that this ambition could be affected by the ambitions in the Local Government devolution and reform White Paper.

The positive news for the Council was the Extended Producer Responsibility (EPR) funding. This is guaranteed minimum and on top of Core Spending Power in 2025/26. The period from 2026/27 is more uncertain. EPR itself does not place any new burdens on Councils, at least not of the scale of the funding provided. Recycling reforms in relation to mandatory food waste and separate fibre collections do place new burdens on Councils, albeit our new contract had been designed to deliver these. These new burdens will need to be funded. The base assumption used in our budget estimates is that our EPR funding allocation will essentially transform in to new burdens funding.

So, in summary, the base funding assumption for future years is based on:

- A Council Tax referendum limit of 3%.
- Net growth in our tax base (after direct costs linked to new properties) of 0.5% per year.
- A Core Spending Power guarantee of 0%, that is applied after Council Tax rate increases and assuming average growth in the tax base.
- EPR funding to be a proxy for waste new burdens funding, and to stay at a flat cash amount (i.e. no inflation).

It is worth noting that the Core Spending Power guarantee in the form above makes the Council Tax referendum limit irrelevant in terms of the funding that the Council will receive. It merely further shifts the burden of our funding to Local Council Taxpayers.

The policy statement referred to shifting grant funding away from Councils that could generate funding through Council Tax. A more positive scenario could be that the Government allowed Councils to keep some of the gains from Council Tax rate increases, on top of the 0% Core Spending Power guarantee. That would help Councils (especially those deemed to be at floor level) with some contribution towards inflationary cost pressures. It would also mean that Council Tax rises would have some local benefit rather than just off-setting reductions in Government funding. If we were able to keep all of the rate gains (at a 3% increase) it would be additional funding of around £400k in 26/27, increasing to over £1.7 million by 2029/30. Note that this would still likely to be a below inflation increase overall, and would not provide any additional population based funding. It might be that Government only let us keep part of the gain and/or limited Council Tax rate increases to 2%. If we are able to keep 1% of gain per year then that would be around £140k in 26/27, and around

£550k by 2029/30. At 2% per year it would be around £270k in 26/27, and around £1.1 million by 2029/30.

A worse case scenario would see the ERP funding being removed, either in one go or over time. Whilst we should expect to receive waste new burdens funding, there are previous examples of such funding either being insufficient initially, or eroded over time (e.g. through the impact of inflation and/or redistribution). For example, the effective new burdens funding could be just £500k by 2029/30.

There are clearly scenarios that could be described as best or worst case scenarios that would fall beyond those already described. However it seems unlikely that negative RSG will return, at the negative end. And it seems there is insufficient overall money to provide more central funding (i.e. not raised from local Council Tax) and still target funding towards areas of higher deprivation.

It is my view that the assumption made is a reasonable one to make with limited information available. As will become a theme through this section 25 report, there will be a need to be ready to react as better information becomes available. That means having a set of plans that are developed and being ready to make decisions that ensures the ongoing sustainability of the Council.

Impact of inflation

Each year, we apply increases to our budgets to reflect forecasts of contract inflation and pay inflation. Contract inflation is usually linked to specific indicators and we use published economic forecasts to predict what these will be. Once we have worked through the initial adjustments for the new waste and street cleansing contracts, we will have two of our big contracts having been recently retendered and greater cost certainty. However we will still be exposed energy price inflation, and the risk that this is above general inflation and/or it acts as a driver for general inflation.

We have estimated pay inflation at 3% in 2025/26 and then 2% per year thereafter. The overall result for the 2024/25 pay inflation was actually slightly less than the 4% estimate. Even with recent pay increases being higher at the lower grades, increases in the National Living Wage still put pressure on further significant pay increases at these grades. This puts direct pressure on the middle grades and maintaining pay differentials, and pressure on the higher grades which have seen lower increases and have tracked even further behind inflation. Whilst I think the current budget assumption is a reasonable one to take (and is consistent with many other Councils), I am concerned that it may turn out to be an under-estimate.

We set our capital budgets over a 10-year time horizon, and therefore our estimates are susceptible to inflation between when they are added to the programme and when the expenditure is ultimately incurred. For more discretionary capital spend, this can have an impact on viability when estimates are updated. For example, the allocation for a pavilion at Walsworth Common is now too low, and there is a need to identify more third party funding to maintain this as a deliverable project (without a much more significant Council contribution). At a more significant level, the allocation for a new waste depot is likely to be insufficient, unless it can be delivered in a different way or with a change in scope of what is required. The estimates will need to be reviewed as we get closer to the need and opportunity to deliver such a project.

Some of the Grounds Maintenance forecasts do not get adjusted (e.g. the play area refurbishment allocations), although the extent of some of these can be adjusted to fit the budget available.

There are some revenue budgets that do not get inflated each year, i.e. budgets that do not relate to pay or where known contract inflation can be applied. These are generally low value budgets that

pay for ad-hoc items, but it is acknowledged that the spending power of those budgets is being eroded. In the quarterly budget monitoring process we have not seen any pattern of overspend against these budgets. Although staff training is one of these budget types, we have generally found creative ways to get the most out of these budgets (e.g. use of our apprentice levy, use of other organisations unused levy). Although this will be kept under review, as it vital that we value staff training.

The inflation that is applied to fees and charges budgets is done in accordance with the assumptions agreed in the MTFS. In some areas this acts as a clear plan for how the level of fees and charges will be adjusted, although there is still uncertainty over the level of demand for those services. For car parking charges there is an additional level of risk over the total income that will be received. The MTFS assumption acts as a budget forecasting estimate only, and there will be a subsequent report to Cabinet to consider the actual changes to parking tariffs. That report will need to consider the wider implications and justification for any tariff changes. Whilst the percentage increase is moderate (2%), the total impact equates to around £50k. I feel that this is a balanced assumption, but there is an element of risk to highlight.

Demand pressures and grant funding

In relation to the potential impact of reduced demand (either at current prices or where prices are inflated), there are various factors that provide me with confidence that the forecasts are reasonable. Firstly, we have been carrying out budget monitoring through the first 8 months of the year and have not seen any significant in-year drops in demand that needs to be adjusted on an ongoing basis. Secondly, whilst the most significant increase in charge is for garden waste (relative to previous increases), the assumptions allow for some drop-off in demand, the charging is in line with or below other Councils and they have not reported any significant falls in demand. Thirdly, the proposed new charging that is proposed is for car parking in the evenings and on Sundays, but the financial impact is currently shown as TBC (which equates to zero) which allows the impact (if adopted following consultation) to only be incorporated when we see the actual impact.

Housing is the main service area where we see demand pressures, which usually result in an increase in the need to use hotel and B&B placements. The excess cost of these placements is currently being covered through specific housing grants, and we have seen an increase in the specific grant that we have been awarded. The conversion of Anderson House (in Hitchin) in to homeless accommodation will also help by increasing the supply, especially for those requiring greater support. But it remains an area to keep a focus on through quarterly monitoring.

As detailed in the main budget report, the risks in relation to other specific grant funding have also been considered.

Capital spend, capital funding and debt

Capital spend comes with a revenue cost, which ranges from lost treasury income through to external interest charges and Minimum Revenue Provision. There is therefore a need to ensure that our capital spend forecasts continue to be realistic, both in terms of cost forecasts for items that are progressing, as well as being prepared to remove those items that are no longer deliverable.

The impact of inflation on capital spend forecasts is considered above. The need to fund capital spend from borrowing comes with an increased revenue cost, compared with being able to fund it from capital receipts. It is therefore necessary to consider the assumptions made in relation to generating new capital receipts.

Recent reports to Council (July 24 and January 25) requesting additional budget for the leisure centre decarbonisation scheme shows that major capital projects are susceptible to capital cost inflation and changes in revenue forecasts (e.g. changes in costs/ income). The second decarbonisation bid is lower value and scale, but there is still the potential for cost increases, and it will need to be kept under review. Whilst the plans for Churchgate area regeneration (in Hitchin) are still being developed, there are options that could make it a very large project. The inherent risk of such a project could require an increase in the recommended minimum General Fund balance, which would reduce the flexibility over the timing of the delivery of savings.

There has been a delay in the timing and amount of capital receipts compared to previous forecasts. This is due to previous vacancies in the Estates team and some site-specific changes that have now come to light. As we have reaching the tipping point where we are running out of existing capital reserves, the Estates team are being prudent in the timing of their forecast receipts. This results in a higher forecast Minimum Revenue Provision charge than may be required, but I consider this to be necessarily prudent.

As it currently stands, we have a small amount of historic external debt that it is not economic to repay. In the short-term we have the option to borrow internally against our revenue reserves and delay any further external borrowing as long as possible. This is both a more prudent approach, and likely to reduce longer term costs as it is likely that the cost of borrowing will reduce in the medium term (although not to the exceptionally low levels seen from 2008-2022).

Savings requirement

The plan (as detailed in the MTF5) is to use Business Rate pooling gains (that are held in reserve) and General Fund reserves to support balancing the budget in 2025/26. This will be further helped by the ERP funding which will reduce the call on those reserves (at least in 2025/26). This is contingent on the commitment to take action during 2025/26 (including public consultation) to make decisions on savings to be implemented in 2026/27 onwards.

As there is not a savings target in place for the current year, any savings that have been put forward have not been due to pressure being placed on Budget Managers. Therefore, I consider the savings that have been put forward as part of this budget to be achievable and I do not need to flag any risks or concerns.

Council Reserves and the CIPFA Resilience Index

At the start of 2025/26 we expect our General Fund reserves to be £14.4m and we also have £6.5m of previous Business Rate gains and grants held in reserve. As detailed in the budget report this is substantially above the recommended Minimum General Fund reserve levels. This gap helps to provide further comfort against the risks and concerns that I have highlighted in this section 25 report.

The Chartered Institute for Public Finance and Accountancy (CIPFA) produce a Resilience Index for Councils. CIPFA recommend that Chief Finance Officers consider the results from the index in compiling their section 25 reports.

The index is published on the CIPFA website (<https://www.cipfa.org/services/financial-resilience-index>). At the time of writing this report the version on the website was still based on March 2023 data. CIPFA had provided a pre-release version using 2024 data to Chief Finance Officers, and the considerations below are based on that version. I hope that version is published on the CIPFA website soon.

The Resilience Index includes some important measures in relation to level of reserves and how quickly they are being used. However, as it is based on data from the previous financial year-end, it obviously is not current data. Any key messages that are highlighted by the Resilience Index, would usually have been being flagged by the Council's Chief Finance Officer long before they show up on the Resilience Index. However, the Index can help as a wake-up call to reiterate the need for action.

The Index is based on comparisons, both with others and over time. In our case we can compare ourselves against all Districts or our statistical near neighbours. This can help with highlighting with where you are different to other Councils and not just rely on the fact that it is difficult for everyone.

When compared with our nearest neighbours the two measures which are showing as higher risk are: change in reserves and level of earmarked reserves. Our results are that our change in reserves was -10% (comparative range of -89% to +29%). However, this is in accordance with our short-term strategy and needs to be considered in the context of our overall level of reserves. Our overall level of reserves (compared with net expenditure) is at the lowest risk level. The story in relation to earmarked reserves is similar and we have been shifting earmarked reserves that aren't really that targeted in to the General Fund. So that would explain the levels and reductions in those levels. My conclusion is that our reserves are at a reasonable level for the risks that we are exposed to. Some Councils may have higher reserves as a way to mitigate against the higher risks (e.g. in relation to investments or borrowing) that they face. There is capacity for our reserves to drop as we respond to the budget pressures that we expect to have to face. But is worth noting that our reserves are not so high to allow for an excessively delayed response. They are at a level that allows for measured but prompt response but reflecting that savings will take some time to implement.

Conclusion

Overall, I consider that the budget is proposed based on robust estimates. I have highlighted where I feel that there are elements of higher risk, but I am satisfied that there are mechanisms in place to be able to respond to these if required.

My overall conclusion is focused on the medium-term. It is almost certain that there will be a need to act. Even the more optimistic projections on funding would require savings to be identified and delivered of over £1m (and more likely in the range £2.5m - £3.5m). There will need to be some difficult decisions over areas of priority during 2025/26, to help inform the 2026/27 budget process. As long as action is taken then the Council can be sustainable in the medium-term and beyond. But if action is not taken then our reserves could fall very quickly. The Corporate Peer Challenge also highlighted the benefits of achieving a balanced budget more quickly and then using any reserves that are deemed to be surplus for investment in the district.