Herefordshire Council

Supplement to the agenda for

Council

Friday 7 February 2025

10.00 am

Conference Room 1 - Herefordshire Council, Plough Lane Offices, Hereford, HR4 0LE

Report of the Chief Financial Officer (S151 Officer) on the robustness of the 2025/26 budget estimates and the adequacy of reserves

Introduction

This report is made under section 25 of the Local Government Act 2003, which the Council is required to have regard to when making decisions in accordance with s.31A of the Local Government Finance Act 1992.

Section 25 of the Local Government Act 2003 requires that the Chief Financial Officer reports the following matters to Council, when approving the budget for the financial year 2025/26:

- the robustness of the estimates made for the purpose of the budget calculations; and
- the adequacy of the proposed financial reserves.

National and Local Financial Risks

Nationally, local authorities continue to face significant financial pressures: increasing costs and demand for services, challenges in recruitment and uncertainty over future funding arrangements, and funding allocations, place the financial resilience of all local authorities under strain.

In recent years, these risks to financial stability have materialised; evidenced through both an increase in the issue of Section 114 notices as well as more widespread implementation of strict expenditure controls to avoid statutory intervention. In some cases, Section 114 notices have been issued as a result of unlawful transactions and historical accounting errors however the scale of financial challenges, largely driven by demand and cost for social care, places the solvency of the sector at risk.

In October 2024, the County Councils Network (CCN) highlighted the impact of rising demand and cost in Special Educations Needs and Disabilities (SEND) services on financial resilience. Unprecedented and exponential increases in Education, Health and Care Plans (EHCPs), surging costs in adult social care, children's services and home to school transport are they key drivers of growing deficits and, without significant reform, these pressures place local authorities at risk of insolvency.

Overview of financial management and governance arrangements

Whilst Herefordshire is not immune to these national issues, the council is in a strong and resilient position to respond to and withstand future financial pressures.   This strong financial position is evidenced through:

- a balanced budget for 2025/26 which includes realistic and achievable savings;
- adequate reserves to manage financial risks and respond to emerging pressures;
- positive cashflow and high levels of liquidity; and
- a strong balance sheet with low levels of borrowing relative to the council's asset base.

The council's financial planning and monitoring arrangements which safeguard the financial sustainability of the council have been reviewed against National Audit Office criteria by external auditors. The Auditor's Annual Report published in September 2024 confirms there are no significant weaknesses in arrangements to ensure the council manages risk to its financial sustainability. This report further confirms that arrangements for identifying, developing, monitoring and reporting on savings are appropriate and that the budget is informed by realistic estimates in key areas.

The council received an unqualified audit opinion on the 2023/24 financial statements in September 2024; the first and only council to achieve this by the statutory deadline. The timely and accurate preparation of the council's statutory accounts is critical in enabling a timely audit to provide valuable, independent assurance of the accuracy and compliance of the council's financial reporting and underlying accounting transactions, estimates and judgements.

Performance against 2024/25 approved Revenue Budget

At Quarter 2 2024/25, the council is forecasting an adverse variance of £10.2 million (4.8% of net budget), before management recovery action which is expected to reduce the forecast overspend to £2.0 million by 31 March 2025. The overspend includes in-year cost pressures of £3.9 million, total 2024/25 savings targets assessed as 'at risk' of £5.0 million, £0.4 million savings targets brought forward from 2023/24 assessed as 'at risk' and a further £2.3 million of council-wide 2024/25 savings targets with activity pending.

In-year cost pressures represent increases in client demand and complexity of care across adult social care budgets and increases in demand for temporary accommodation in the Community Wellbeing Directorate, under-delivery of development planning income in the Economy & Environment Directorate and an increase in external audit fees in Corporate Services. In addition, the council faces significant pressures in the provision of mainstream home to school transport and SEND transport services and a review has been commissioned by the Chief Executive to introduce a new operating model for transport services in 2025/26. The timely delivery of actions to deliver efficiencies in transport services is critical to manage cost pressures in future years.

The proposed budget for 2025/26 addresses each of these areas to ensure that the budget allocations are sufficient to meet the costs of service delivery.

To deliver services within the approved budget in 2025/26, continuing robust financial management and responsible stewardship of resources is essential, particularly in areas of high-risk activity and demand led services. Whilst estimates of the required budget in these areas is based on reasonable and appropriate assessments of costs and volume, there is a risk that these estimates will be exceeded. The Budget Resilience Reserve has been established in 2024/25 to manage and mitigate the impact of in-year cost pressures and volatility in demand across social care budgets in 2025/26 and future years. This demonstrates a prudent approach to managing the risk of uncertainty in an area which represents a significant national challenge.

Expenditure controls will remain in place throughout 2025/26. Directorate panels will continue to review expenditure on goods and services as well as changes in staffing arrangements to maintain an increased level of rigour and challenge over expenditure. Timely budget monitoring and collaboration between service and finance teams to support accurate forecasting will highlight adverse variances and emerging costs pressures, enabling prompt management action to mitigate risks to in-year delivery within budget.

Delivery of Savings

The 2024/25 approved revenue budget included a savings target of £19.5 million comprising Directorate savings of £11.6 million and council-wide savings of £7.9 million across a range of proposals to transform services, reduce expenditure, increase opportunities for cost recovery and review the size and shape of the organisation.

The delivery of savings at a time of increasing demand and budget pressures remains a significant challenge for the council. The Quarter 2 2024/25 Budget Report presented to Cabinet in November 2024 reports forecast delivery of £14.5 million (74% of total savings) in 2024/25 with the balance of £5.0 million assessed as 'at risk'. Savings of £0.4 million brought forward from the 2023/24 financial year are also assessed as 'at risk'. Whilst work continues over the remainder of the financial year to maximise delivery of these savings or identify mitigations, the delivery of recurrent savings, in full and on-time, is critical to ensuring a balanced revenue outturn position to prevent risk to the council's reserves and pressure on future years' budgets.

Dedicated Schools Grant (DSG)

The cumulative DSG deficit is accounted for as an unusable reserve on the council's Balance Sheet, as permitted via statutory instrument, which will remain in place until 31 March 2026. This enables all local authorities to ring-fence the DSG deficit from the overall financial position in the statutory accounts.

Herefordshire, like many other local authorities, continues to experience increases in demand which are not met by corresponding increases in funding and the number of authorities with significant DSG deficits is increasing. If the statutory override is not extended, the expectation is that any balance will become a liability of the council. This remains a significant risk for the council with a forecast deficit at Q2 of 2024/25 of £7.6 million within the High Needs block of the DSG; increasing the cumulative deficit to £13.7 million by 31 March 2025. A focused review to quantify the impact of emerging demand in 2025/26 and future years is currently underway to inform the council's DSG Deficit Management Plan. It is expected that this will increase the forecast deficit by 31 March 2025.

It is critical that action is taken to address this deficit and the council continues to work with the Department of Education to monitor delivery of the DSG Deficit Management Plan as well as the Local Government Association and other local authorities to seek clarification on the position once the statutory instrument expires.

Robustness of estimates

The development of the 2025/26 Revenue Budget and 2025/26 to 2028/29 Medium Term Financial Strategy (MTFS) has been led by the council's Finance Team working collaboratively with Directorate Leadership Teams, the Corporate Leadership Team and Cabinet.

All key assumptions and areas of estimation and judgment which inform the budget, savings, income, inflation, growth bids and capital projects have been subject to review and challenge as part of the budget setting process in 2025/26. Directorate budget proposals, savings plans and capital project business cases have been assessed alongside the impact of emerging cost pressures and relevant activity data in 2024/25, to inform the production of the 2025/26 revenue budget.

There has been increased engagement in the budget setting process for 2025/26 achieved through regular communication with stakeholders, sharing of information and increased transparency in respect of estimates, judgements and assumptions which inform the budget. Regular updates of progress in development of the budget have been shared with local MPs, Cabinet, Corporate Leadership Team, Leadership Group and council staff through routine All Staff Briefing sessions. Members and Group Leaders have received regular briefings where the challenges of balancing cost pressures with reduced Central Government funding have been discussed by all political groups.

This approach in 2025/26 has supported an informed and effective scrutiny of the revenue budget and capital programme, evidenced through both the formal scrutiny process as well as through increased requests for information, clarity and explanation of proposals from Members and Officers.

The assumptions which inform the 2025/26 budget and MTFS are explained in Table 2 of the MTFS, included at Appendix B to the Budget Report. Assumptions have been developed and assessed by the Finance Team with support from specialist external advisors and professional networks. Estimates are based on historical experience, current trends and other relevant factors. Financial forecasts are monitored as part of routine budget monitoring arrangements to ensure that risks are identified in a timely manner and mitigation action is taken.

Adequacy of reserves

An assessment to confirm the adequacy and robustness of reserve balances has been undertaken as part of the budget setting process for 2025/26. The Earmarked Reserves and General Policy Statement 2025/26, sets out the council's approach to maintaining appropriate levels of reserves and general balances to meet known future commitments and to mitigate against unforeseen future events.

The council's financial strategy aims to minimise the use of reserves in the medium term and to replenish them to support future sustainability, enable the council to respond to unexpected changes and to invest in the continued transformation and improvement of its services.

There are robust controls in place, as part of routine budget monitoring arrangements, to monitor in-year transfers to and from reserves and resulting reserve balances and these transactions are subject to review as part of the annual audit of the statutory accounts.

The Chartered Institute of Public Finance and Accountancy (CIPFA) Financial Resilience Index is a comparative tool to support good financial management. The index shows a council's position on a range of measures associated with financial risk to highlight where additional scrutiny may be required. The data for the most recent index reflects figures obtained from the Revenue Expenditure and Financing England Outturn Report 2023/24 (RO Forms) as at 31 March 2024.

The reserve sustainability measure provides a measure of how long in years it will take for a council to run out of reserves if they continue to use them as they have and the associated level of risk. This data highlights the council's reserve sustainability measure to be 'lower risk' and notes the council has average reserves relative to its nearest neighbour and other unitary authority comparator groups.

The risk assessment for 2025/26 has determined that a General Fund balance of £9.6 million, unchanged from 2024/25, should be maintained. This is equivalent to 4.1% of the proposed operating budget of £231.5 million for 2025/26 and equates to between two and three weeks of net expenditure. I consider this to be an adequate working balance.

The Annual Review of Earmarked Reserves 2024/25 and Earmarked Reserves and General Policy Statement 2025/26 was reported to Cabinet in January 2025. A full schedule of Earmarked Reserve balances, including forecast use to 31 March 2026, is included at Appendix E to the Budget Report.

Statement of Chief Financial Officer (S151 Officer) Opinion

In discharging governance and monitoring roles, Members are asked to consider the financial risks highlighted and the actions required to manage expenditure within the proposed budget and preserve the council's financial position.

Section 25 of the Local Government Act 2003 requires the Chief Financial Officer (S151 Officer) to report to Council on the robustness of estimates and adequacy of reserves and requires that Council have regard to this report in approving the budget recommended by Cabinet.

This report sets out my assessment of the national and local risks to the delivery of the 2025/26 budget and the financial resilience of the council. In consideration of these risks, it is my opinion that:

- estimates used in the revenue budget and capital programme for 2025/26 are robust, informed by reasonable and realistic assumptions and judgements;
- forecast earmarked reserve and general balances are adequate to manage future risks and uncertainties facing the council;
- savings proposed in the 2025/26 revenue budget are realistic and achievable; and
- appropriate actions have been identified to respond to areas of high risk to the council's budget and there are robust arrangements to monitor delivery.

Rachael Sanders
Director of Finance (S151 Officer)